HALIFAX

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Item No.
Audit & Finance Standing Committee
March 8, 2017

TO:	Chair and Members of Audit & Finance Standing Committee
SUBMITTED BY:	Original Signed Amanda Whitewood, Director of Finance & ICT / CFO
DATE:	February 27, 2017
SUBJECT:	**Audit of the Consolidated Financial Statements of HRM**

ORIGIN

This report is originated by staff in preparation for the 2017 year end audit of the consolidated financial statements of HRM.

LEGISLATIVE AUTHORITY

Section 46 of the Halifax Regional Municipality Charter outlines the responsibilities of the Municipal Auditor including issuance of an Auditor's Report.

RECOMMENDATION

It is recommended that the Audit & Finance Standing Committee approve the attached Audit Planning report for the year end audit of HRM's consolidated financial statements as prepared by the Municipal Auditor (KPMG).

BACKGROUND

Each year the Municipal Auditor is required to prepare an Audit Planning Report to be approved by the Audit & Finance Standing Committee.

DISCUSSION

KPMG has prepared the attached Audit Planning Report for review and approval by the Audit & Finance Standing Committee.

FINANCIAL IMPLICATIONS

The fees for the year end audit, as described in the Audit Planning Report are consistent with the amount in the tender and are budgeted for.

RISK CONSIDERATION

There are no significant risks associated with the recommendation in this report. The risks considered rate Low. To reach this conclusion, consideration was given to operational and financial risks.

COMMUNITY ENGAGEMENT

None required.

ENVIRONMENTAL IMPLICATIONS

Implications not identified.

ALTERNATIVES

The Audit & Finance Standing Committee through discussion with our Municipal Auditor, may request additional services or audit procedures. These services or audit procedures would likely be a separate engagement and would result in increased costs to HRM.

ATTACHMENTS

1. KPMG's Audit Planning Report for the March 31, 2017 year end audit of the consolidated financial statements of HRM.

A copy of this report can be obtained online at http://www.halifax.ca/commcoun/index.php then choose the appropriate Community Council and meeting date, or by contacting the Office of the Municipal Clerk at 902.490.4210, or Fax 902.490.4208.

Report Prepared by: Diana Burns, Senior Financial Consultant, Financial Reporting, 902.490.6315

Report Approved by: Original Signed
Louis de Montbrun, Manager of Financial Reporting, 902.476.0585

Financial Approval by: Original Signed
Amanda Whitewood, Director of Finance & ICT / CFO, 902.490.6308

Halifax Regional Municipality

Audit Planning Report

For the year ended March 31, 2017

KPMG LLP

February 28, 2017

kpmg.ca/audit

The contacts at KPMG in connection with this report are:

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Table of contents

Executive summary	**3**
Audit approach	**4**
Data & analytics in the audit	**9**
Materiality	**10**
Value for fees	**11**
Appendices	**12**

At KPMG, we are **passionate** about earning your **trust**. We take deep **personal accountability**, individually and as a team, to deliver **exceptional service and value** in all our dealings with you.

At the end of the day, we measure our success from the **only perspective that matters – yours**.

Executive summary

Audit and business risk

Our audit is risk-focused. In planning our audit we have taken into account key areas of focus for financial reporting.

See pages 5 – 8 and Appendix 2.

KPMG team

The KPMG team will be led by Carey Blair. Subject matter experts will be involved to ensure our approach is appropriate and robust.

Effective communication

We are committed to transparent and thorough reporting of issues to **Diana Burns**, Senior Financial Consultant, Accounting – Financial Reporting, **Louis de Montbrun**, Manager Financial Reporting, **Amanda Whitewood**, Director of Finance and Information, Communication and Technology/ CFO and the **Audit and Finance Standing Committee**.

Audit materiality

Materiality has been determined based on revenues. We have reviewed the scope of work across segments and businesses across the group. Materiality will be set at lower thresholds where necessary to meet governmental unit and associated financial statement audit requirements. We have determined group materiality to be $14,400,000 for the year ending March 31, 2017.

See page 10.

Independence

We are independent and have extensive quality control and conflict checking processes in place.
See Appendix 1.

Current developments

Please refer to Appendix 7 for relevant accounting and/or auditing changes that may be relevant to the Halifax Regional Municipality.

Audit approach

Inherent risk 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.

Our assessment of inherent risk is based on various factors, including the size of the balance, its inherent complexity, the level of uncertainty in measurements, as well as significant external market factors or those particular to the internal environment of the entity.

Significant financial reporting risks	Why	Our audit approach	
We have not identified any significant reporting risks or unusual transitions.			

Audit approach

Professional standards presume the risk of fraudulent revenue recognition and the risk of management override of controls exist in all companies.

The risk of fraudulent revenue recognition can be rebutted, but the risk of management override of control cannot, since management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Professional requirements	Why	Our audit approach
Fraud risk from revenue recognition	This is a presumed fraud risk. Fraud risk has been rebutted as the Halifax Regional Municipality ("HRM") prepares consolidated financial statements using Public Sector Accounting Standards. Key decisions such as tax rates and service fees are based on guidance in the Nova Scotia Municipal Government Act. There are no incentives or bias to report higher or lower revenue.	N/A
Fraud risk from management override of controls	This is a presumed fraud risk. We have not identified any specific additional risks of management override relating to this audit.	As the risk is not rebuttable, our audit methodology incorporates the required procedures in professional standards to address this risk. These procedures include testing of journal entries and other adjustments, performing a retrospective review of estimates and evaluating the business rationale of significant unusual transactions.

Audit approach

Other areas of focus include the following:

Other areas of focus	Why	Our audit approach	Component
Taxation Revenues	Most significant revenue source for the HRM.	Evaluating the design and implementation of controls and complete substantive analytical procedures over the completeness, existence and accuracy of additions to revenue based on assessed property values.	Not Applicable
Capital Expenditures	HRM is engaged in significant capital projects annually.	Evaluating the design and implementation and operating effectiveness of controls over procurement. Complete substantive procedures over the completeness, existence and accuracy of additions to capital assets.	Not Applicable
Change in investment in Halifax Regional Water Commission ("HRWC")	HRWC is a significant investment accounted for on the Modified Equity basis.	Direct, review and communicate with HRWC's auditor and have them report findings to KPMG.	Provide written instructions to HRWC auditor

User fees and charges	Significant source of revenue for the HRM	Evaluating the design and implementation of controls and complete substantive analytical procedures over the completeness, existence and accuracy of revenue.	Desktop review of significant Associations, Boards and Commissions (“ABCs”).
Payroll expenditures	HRM payroll is a significant expense across all functions	Evaluating the design and implementation and operating effectiveness of controls over payroll. Perform substantive procedures including substantive analytical procedures over the completeness, existence and accuracy of payroll expense.	Desktop review of significant ABC’s.
Routine expenditures	Procurement is a significant function of the HRM supporting all functions	Evaluating the design and implementation and operating effectiveness of controls over procurement. Perform substantive procedures including substantive analytical procedures over the completeness, existence and accuracy of routine expenditures.	Not Applicable
Treasury	Cash and borrowing is significant to the financial position.	Evaluating the design and implementation of controls and complete substantive procedure through external confirmation over cash and debt balances.	Not Applicable

Audit approach

Professional standards require that we obtain an understanding of the entity's organizational structure, including its components and their environments, that is sufficient to identify those components that are financially significant or that contain specific risks that must be addressed during our audit.

Group auditors are required to be involved in the component auditors' risk assessment in order to identify significant risks to the group financial statements. If such significant risks are identified, the group auditor is required to evaluate the appropriateness of the audit procedures to be performed to respond to the identified risk.

The components over which we plan to perform audit procedures are as follows:

Components	Why	Our audit approach
Halifax Regional Water Commission (HRWC) Grant Thornton, Halifax	Individually financially significant	Statutory audit of component financial statements (see previous).
Canada Games Centre, Dartmouth Sportsplex, Scotiabank Centre, Halifax Regional Library and Community Builders Inc. KPMG, Halifax	Non-significant components	Review of component financial information through consolidation work.
Sackville Sport Stadium and BMO Centre KPMG, Halifax	Non-significant components	Included in the financial information of the HRM non-consolidated therefore no further work required.
All other ABCs are not considered financially significant to the consolidated financial statements.		

Data & analytics in the audit

We will be integrating Data & Analytics (D&A) procedures into our planned audit approach.

Use of innovative D&A allows us to analyze greater quantities of data, dig deeper and deliver more value from our audit.

We believe that D&A will improve both the quality and effectiveness of our audit by allowing us to analyze large volumes of financial information quickly, enhancing our understanding of your business as well as enabling us to design procedures that better target risks.

Area(s) of focus	Planned D&A routines
Journal entry testing	– Utilizing KPMG application software (IDEA) to evaluate the completeness of the journal entry population through a roll-forward of accounts. – Utilizing computer-assisted audit techniques (CAATs) to analyze journal entries and apply certain criteria to identify potential high-risk journal entries for further testing.

Detailed results and summary insights gained from D&A will be shared with management and presented in our Audit Findings Report.

Materiality

Professional standards require us to re-assess materiality at the completion of our audit based on period-end results or new information in order to confirm whether the amount determined for planning purposes remains appropriate.

Our assessment of misstatements, if any, in amounts or disclosures at the completion of our audit will include the consideration of both quantitative and qualitative factors.

The first step is the determination of the amounts used for planning purposes as follows.

The determination of materiality requires professional judgment and is based on a combination of quantitative and qualitative assessments including the nature of account balances and financial statement disclosures.

Materiality determination	Comments	Group amount
Metrics	Total Revenue, Total Expenses and Net assets	
Benchmark	Total Revenue	$960 million
Materiality	Determined to plan and perform the audit and to evaluate the effects of identified misstatements on the audit and of any uncorrected misstatements on the financial statements. The corresponding amount for the prior year's audit was $14.28 million.	$14.4 million
% of Benchmark	The corresponding percentage for the prior year's audit was 1.5%.	1.5%
Performance materiality	Used 75% of materiality, and used primarily to determine the nature, timing and extent of audit procedures. The corresponding amount for the prior year's audit was 75%.	$10.8 million
Audit Misstatement Posting Threshold (AMPT)	Threshold used to accumulate misstatements identified during the audit. The corresponding amount for the previous year's audit was $714,000.	$720,000
	HRM – Non-consolidated	HRWC
Component Materiality	$13 million	$7.2 million

Value for fees

In determining the fees for our services, we have considered the nature, extent and timing of our planned audit procedures as described above. Our fee analysis has been reviewed with and agreed upon by management.

Our fees are estimated as follows:

	Current period (budget)	Prior period (actual)
Audit of the annual consolidated financial statements	$82,750	$80,300

Matters that could impact our fee

The proposed fees outlined above are based on the assumptions described in the engagement letter. The critical assumptions, and factors that cause a change in our fees, include:

- Significant changes in the nature or size of the operations of the HRM beyond those contemplated in our planning processes;
- Changes in professional standards or requirements arising as a result of changes in professional standards or the interpretation thereof; and
- Changes in the time of our work.

Appendices

Appendix 1: Audit quality and risk management

Appendix 2: KPMG's audit approach and methodology

Appendix 3: Required communications

Appendix 4: Data & analytics in audit

Appendix 5: Lean in Audit™

Appendix 6: Expanded Auditor Reporting

Appendix 7: Current developments

Appendix 1: Audit quality and risk management

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

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

Visit our Audit Quality Resources page for more information including access to our audit quality report, Audit quality: Our hands-on process.

- Other controls include:
  - Before the firm issues its audit report, Engagement Quality Control Reviewer reviews the appropriateness of key elements of publicly listed client audits.
  - Technical department and specialist resources provide real-time support to audit teams in the field.
- We conduct regular reviews of engagements and partners. Review teams are independent and the work of every audit partner is reviewed at least once every three years.
- We have policies and guidance to ensure that work performed by engagement personnel meets applicable professional standards, regulatory requirements and the firm's standards of quality.

- All KPMG partners and staff are required to act with integrity and objectivity and comply with applicable laws, regulations and professional standards at all times.
- We do not offer services that would impair our independence.
- The processes we employ to help retain and develop people include:
  - Assignment based on skills and experience;
  - Rotation of partners;
  - Performance evaluation;
  - Development and training; and
  - Appropriate supervision and coaching.
- We have policies and procedures for deciding whether to accept or continue a client relationship or to perform a specific engagement for that client.
- Existing audit relationships are reviewed annually and evaluated to identify instances where we should discontinue our professional association with the client.

Appendix 2: KPMG's audit approach and methodology

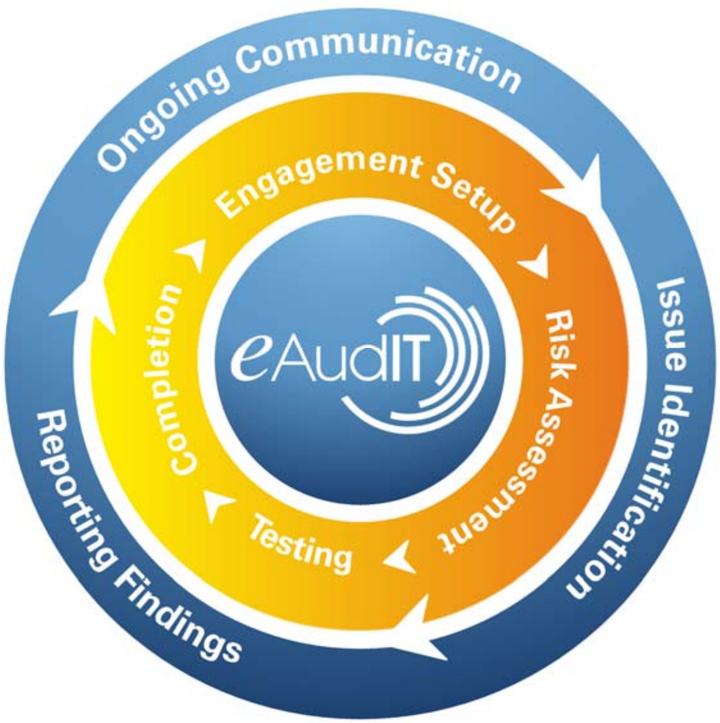
Technology-enabled audit workflow (eAudIT)

Engagement Setup

- Tailor the eAudIT workflow to your circumstances
- Access global knowledge specific to your industry
- Team selection and timetable

Completion

- Tailor the eAudIT workflow to your circumstances
- Update risk assessment
- Perform completion procedures and overall evaluation of results and financial statements
- Form and issue audit opinion on financial statements
- Obtain written representation from management
- Required Audit and Finance Standing Committee communications
- Debrief audit process



Risk Assessment

- Tailor the eAudIT workflow to your circumstances
- Understand your business and financial processes
- Identify significant risks
- Plan the use of KPMG specialists and others including auditor's external experts, management experts, internal auditors, service organizations auditors and component auditors
- Determine audit approach
- Evaluate design and implementation of internal controls (as required or considered necessary)

Testing

- Tailor the eAudIT workflow to your circumstances
- Perform tests of operating effectiveness of internal controls (as required or considered necessary)
- Perform substantive tests

Appendix 3: Required communications

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

- **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 and any subsequent amendment letters as provided by management.
- A**udit planning report** – as attached
- **Required inquiries** – professional standards require that during the planning of our audit we obtain your views on risk of fraud and other matters. We make similar inquiries to management as part of our planning process; responses to these will assist us in planning our overall audit strategy and audit approach accordingly
- **Management representation letter** – we will obtain from management certain representations at the completion of the annual audit. In accordance with professional standards, copies of the representation letter will be provided to the Audit and Finance Standing Committee
- **Audit findings report** – at the completion of our audit, we will provide a report to the Audit and Finance Standing Committee

Appendix 4: Data & analytics in audit

Turning data into value

KPMG continues to make significant investments in our Data & Analytics (D&A) capabilities to help enhance audit quality and provide actionable insight to our clients by unlocking the rich information that businesses hold.

When D&A is applied to the audit, it enables us to test complete data populations and understand the business reasons behind outliers and anomalies. Advancements in D&A tools allow us to analyze data at more granular levels, focusing on higher risk areas of the audit and developing insights you can then leverage to improve compliance, potentially uncover fraud, manage risk and more.

KPMG is enhancing the audit

The combination of our proven industry experience, technical know-how and external data allows us to focus our audit on the key business risks, while providing relevant insights of value to you.

For the audit

Audit quality

– Automated testing of 100% of the population

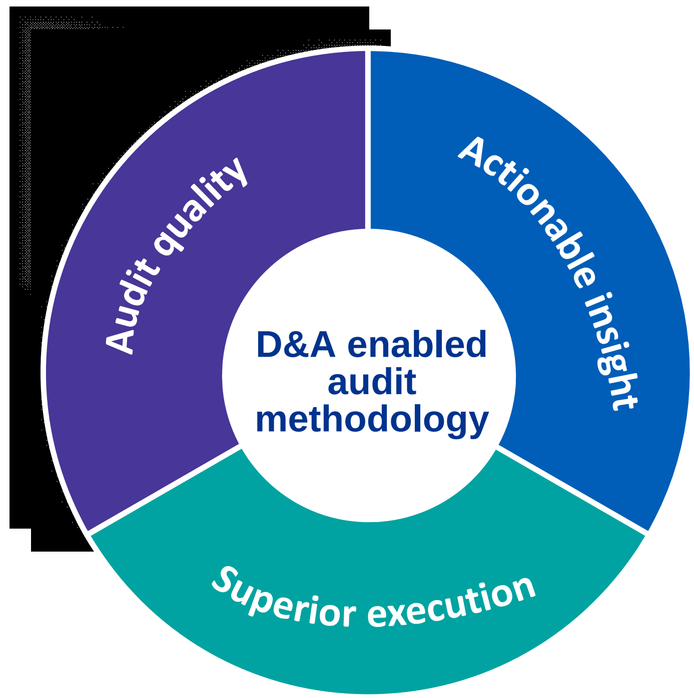
– Focuses manual audit effort on key exceptions and identified risk areas

For your business

Actionable insight

– Helping you see your business from a different perspective

– How effectively is your organization using your systems?



Appendix 5: Lean in Audit™

An innovative approach leading to enhanced value and quality

Our new innovative audit approach, Lean in Audit, further improves audit value and productivity to help deliver real insight to you. Lean in Audit is process-oriented, directly engaging organizational stakeholders and employing hands-on tools, such as walkthroughs and flowcharts of actual financial processes.

By embedding Lean techniques into our core audit delivery process, our teams are able to enhance their understanding of the business processes and control environment within your organization – allowing us to provide actionable quality and productivity improvement observations.

Any insights gathered through the course of the audit will be available to both engagement teams and yourselves. For example, we may identify control gaps and potential process improvement areas, while companies have the opportunity to apply such insights to streamline processes, inform business decisions, improve compliance, lower costs, increase productivity, strengthen customer service and satisfaction and drive overall performance.

How it works

Lean in Audit employs three key Lean techniques:

1. End-to-end process mapping

- This is a workshop-based approach involving those who actually deliver the process, resulting in a shared, detailed understanding of the process and of client-identified areas of opportunity

2. Visual management

- Providing transparent, real-time reporting ensures a shared understanding of audit priorities, progress and any risks or issues that should be managed, resulting in a more productive, project-led approach that supports client and KPMG efficiencies.

3. Quality and value-mindset

- New capabilities allow audit teams to deliver deeper insights and focus on quality and value.

Appendix 6: Expanded Auditor Reporting

In response to investors demanding more than a binary pass/fail opinion from the auditors' report, the new and revised auditor reporting standards have introduced significant changes to the traditional report we provide.

What's new?

The new standards are intended to provide greater insight and transparency for users of financial statements.

The most significant changes to the audit report impacting listed entities include:

- description of key audit matters; and
- disclosure of the name of the engagement partner.

Other changes impacting listed and non-listed entities include moving the audit opinion to the first section of the report and expanding descriptions of the auditors' and management's responsibilities with respect to the audited financial statements.

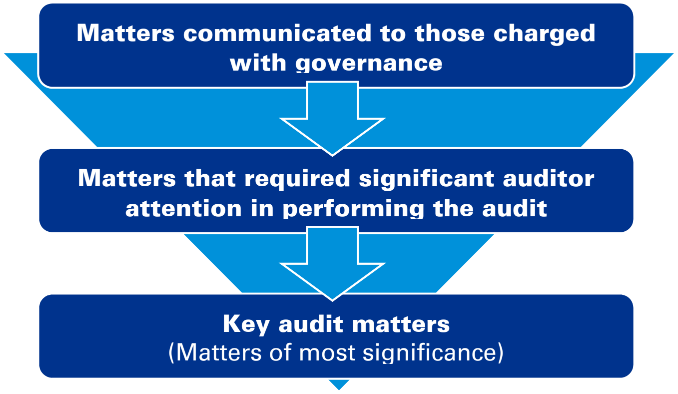
When are the new requirements effective?

While the new standards have already been issued by the International Auditing and Assurance Standards Board, effective for 2016 calendar year-end, they have yet to be adopted as Canadian Auditing Standards (CASs).

The Auditing and Assurance Standards Board in Canada continues to deliberate the new standards including possible effective dates and whether to allow for early application. It is expected, however, that the new auditor reporting standards will be approved in late 2016/early 2017 with an effective date of 2018 calendar year-end audits with possible staggered implementation for certain types of entities.

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements of the current period.

We will be required to include in our auditors' report why the key audit matter is of most significance and what procedures we performed to address the matter.



Appendix 7: Current developments

The following is a summary of the current developments that are relevant to the HRM.

The Public Sector Accounting Board of Canada is responsible for setting the accounting standards that your organization is required to apply in preparing the general purpose financial statements. **The following new or revised accounting standards approved by the Board may have an impact on your financial statements over the next two years as described below.** We encourage Management to review these standards and determine whether the impact, if any, on your organization's financial statements.

In addition, we provide a summary of the status of the Board's deliberations on the future of accounting standards for government not-for-profit organizations. KPMG will continue to update you as these deliberations progress.

Summary of New and Revised Accounting Standards

Assets

PSAB issued Section PS3210 Assets which provides a definition of assets. Assets are defined as follows:

- Assets embody future economic benefits that involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows, or to reduce cash outflows.
- The public sector entity can control the economic resource and access to the future economic benefits.
- The transaction or event giving rise to the public sector entity's control has already occurred.

The standard also includes disclosure requirements related to economic resources that are not recorded as assets to provide the user with better information about the types of resources available to the public sector entity. This standard is effective for fiscal periods beginning on or after April 1, 2017.

Contingent Assets

PSAB issued Section PS 3320 Contingent Assets which defines and establishes disclosure standards for contingent assets. Contingent assets have two basis characteristics:

- An existing condition or situation that is unresolved at the financial statement date.
- An expected future event that will resolve the uncertainty as to whether an asset exists.

The standard also has specific disclosure requirements for contingent assets when the occurrence of the confirming event is likely. This standard is effective for fiscal periods beginning on or after April 1, 2017.

Contractual Rights

PSAB issued Section PS 3380 Contractual Rights which defines contractual rights to future assets and revenue and establishes disclosure requirements. Information about a public sector entity's contractual rights should be disclosed in notes or schedules to the financial statements and should include descriptions about their nature and extent and the expected timing. The standard also indicates that the exercise of professional judgment would be required when determining contractual rights that would be disclosed.

Factors to consider include, but are not limited to:

(a) contractual rights to revenue that are abnormal in relation to the financial position or usual business operations; and

(b) contractual rights that will govern the level of certain type of revenue for a considerable period into the future.

This standard is effective for fiscal periods beginning on or after April 1, 2017.

Related Party Transactions

PSAB issued Section PS 2200 Related Party Transactions which defines related party and provides disclosures requirements. Related parties could be either an entity or an individual. Related parties exist when one party has the ability to control or has shared control over another party. Individuals that are key management personnel or close family members may also be related parties.

Disclosure is only required when the transactions or events between related parties occur at a value different from what would have been recorded if they were not related and the transactions could have a material financial impact on the financial statements. Material financial impact would be based on an assessment of the terms and conditions underlying the transaction, the financial materiality of the transaction, the relevance of the information and the need for the information to enable the users to understand the financial statements.

This standard also specifies the information required to be disclosed including the type of transactions, amounts classified by financial statement category, the basis of measurement, and the amounts of any outstanding items, any contractual obligations and any contingent liabilities. The standard also requires disclosure of related party transactions that have occurred where no amounts has been recognized.

This standard is effective for fiscal periods beginning on or after April 1, 2017. In conjunction with the approval of this standard, PSAB approved the withdrawal of Section PS 4260, Disclosure of Related Party Transactions by Not-for-Profit Organizations, effective for fiscal periods beginning on or after April 1, 2018. Government not-for-profit organizations currently applying Section PS 4260, will therefore only be required to adopt the new standard in their fiscal period beginning on or after April 1, 2018.

Inter-entity Transactions

PSAB issued Section PS 3420 Inter-entity Transactions that specifies how to account for transactions between public sector entities within the government reporting entity. This standard relates to the measurement of related party transactions for both the provider and the recipient and includes a decision tree to support the standard. Transactions are recorded a carrying amounts with the exception of the following:

- Transactions in the normal course of business are recorded at exchange amount
- Transactions with fair value consideration are recorded at exchange amount
- Transfer of an asset or liability at nominal or no consideration is recorded by the provider at carrying amount and the recipient has the choice of either carrying amount or fair value.
- Cost allocations are reported using the exchange amount and revenues and expenses are reported on a gross basis.
- Unallocated costs for the provision of goods or services may be recorded by the provider at cost, fair value or another amount dictated by policy, accountability structure or budget practice

This standard is effective for fiscal periods beginning on or after April 1, 2017. In conjunction with the approval of this standard, PSAB approved the withdrawal of *Section PS 4260, Disclosure of Related Party Transactions by Not-for-Profit Organizations,* effective for fiscal periods beginning on or after April 1, 2018. Government not-for-profit organizations currently applying Section PS 4260 will therefore only be required to adopt the new standard in their fiscal period beginning on or after April 1, 2018.

Deliberations on the Future of Accounting Standards for Not-for-Profit Organizations

In April 2013, the Accounting Standards Board ("AcSB") and the Public Sector Accounting Board ("PSAB") jointly issued a Statement of Principles ("SOP") that proposed to revise Part III of the CPA Canada Handbook and the CPA Public Sector Accounting Handbook to streamline and improve the existing standards for financial reporting by not-for-profit organizations and Government not-for-profit organizations. The SOP garnered much interest from the Not-for-Profit community and, based on the feedback the Boards received, the proposals did not proceed further through the accounting standards development process. In March 2015, citing different financial reporting challenges, user needs and differing priorities faced by PSAB and the AcSB, the Boards announced that they would independently pursue improvements to not-for-profit accounting standards, but collaborate on common issues.

Based on the responses from the SOP, the Public Sector Accounting Board decided that making substantive changes to the Accounting Standards for Government Not-for-Profit Organizations was not a priority at this time. The Board's long-term strategy is to better align the accounting standards used by not-for-profit organizations (as provided in the Section 4200 series in the Accounting Handbook) with those used by other government entities, where practical.

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