

Financial Statement Guide

A Guide to Local Government Financial Statements



January, 2012



Ministry of
Community, Sport and
Cultural Development

Table of Contents

Introduction

Legislative Requirements and Reporting Standards **3**

The Quick Guide to Municipal Financial Statements **4**

Sample Financial Statements

Statement of Financial Position

Sample

Statement of Operations

Sample

Statement of Changes in Net Debt

Sample

Statement of Cash Flows

Sample

Financial Statement Questions and Explanations **13**

Glossary of Terms **18**

Introduction

The guide to Local Government Financial Statements has been prepared by the Ministry of Community, Sport and Cultural Development (Ministry) to help the non-financial reader understand the information presented in local government audited financial statements. The guide provides examples and explanations of the information generally contained in a local government's annual audited financial statements.

The guide provides a brief background about the legislative requirements and financial reporting standards local governments in British Columbia are required to follow, an overview and explanation of the consolidated financial statements that comprise the annual audited financial statement package, answers to commonly asked questions about financial statements and a glossary that provides definitions for many of the terms found in this guide.

Consolidated financial statements report a local government's financial position and its financial performance during a given year. They are a key source of information for elected officials who are then able to make informed decisions about how best to use the local government's fiscal resources to serve the interests of the community.

The consolidated financial statements also establish transparency around a local government's financial position for a given year and provide a measure of accountability to taxpayers. Local government financial statements also demonstrate how well the local government managed its budget over the course of the year and specifically how the taxes and fees citizens paid to the local government were used.

Note: The term "consolidated financial statements" used throughout the guide includes financial information for both the local government and all of the organizations it owns or controls, such as a utility company or a municipal police board.

Legislative Requirements and Reporting Standards

The *Local Government Act* (section 814(3)) and the *Community Charter* (Part 6) require that every local government in British Columbia prepare consolidated financial statements each fiscal year (local governments in B.C. use the calendar year as their fiscal year).

The consolidated financial statements must be prepared by a local government's financial officer in accordance with generally accepted accounting principles for local government. These principles are established by the Public Sector Accounting Board (PSAB), a division of the Canadian Institute of Chartered Accountants (CICA), and are the same for all levels of government everywhere in Canada. The statements must be audited by a qualified auditor – an independent accountant authorized to be an auditor under section 205 of the *Business Corporations Act*. The audited statements must be presented to council and be available for public viewing before June 30. A copy of the audited financial statements must also be submitted to the Ministry by May 15 each year.

The independent auditor reviews the accuracy and completeness of the consolidated financial statements prepared by the local government financial officer; the auditor then provides an audit opinion on the statements. The opinion may be:

- **unqualified** – the auditor has determined the statements are presented in conformity with established standards;
- **qualified** – the auditor has identified one or more specific issues regarding the financial statement preparation;
- **adverse** – the auditor has identified significant issues in the preparation or accuracy of the consolidated financial statement;

If an auditor is unable to examine enough of the financial information to form an opinion about the consolidated financial statements, a denial of opinion may be issued.

The auditor’s opinion is included in a report that can be found at the front of every audited financial statement package.

What’s included in a Consolidated Financial Statement?

Local government consolidated financial statements must include the following four statements:

- Consolidated Statement of Financial Position;
- Consolidated Statement of Operations;
- Consolidated Statement of Changes in Net Debt; and,
- Consolidated Statement of Cash Flow.

Additional information about specific financial statement items is provided in schedules and notes to the financial statements. The notes and schedules provide additional information related to specific line items and figures contained in one or more of the statements and form an integral part of the financial statement package.

The Quick Guide to Municipal Financial Statements

A sample page showing each of the four main elements of the financial statements follows this section, with a set of explanatory notes and hints on the facing page for each one. Each term on the sample page has been **bolded and highlighted** with the corresponding term of the sample financial statement.

There is also a series of questions and answers that may assist in the understanding of these documents. A glossary of terms is included at the end of the document.

Sample Financial Statements

The Ministry has prepared a set of model financial statements. The set includes the four main statements, a comprehensive presentation of typical notes to a set of financial statements and supplementary schedules. This complete package is available online from the Ministry website at:

http://www.cscd.gov.bc.ca/lgd/infra/library/Model_Financial_Statements.pdf

Consolidated Statement of Financial Position

The Consolidated Statement of Financial Position provides key details about a local government's assets, liabilities and any accumulated surplus for a given fiscal year. It can be a general indicator of a local government's long-term financial health; however, it is much more than an accounting of the amount of the money a local government has in the bank. The statement of financial position gives the best indication whether or not a local government has the necessary assets to provide services to its residents in the future and meet its current financial commitments.

There are four key elements of a financial position statement.

Financial Assets – are those current cash resources plus any items that are expected to be converted into cash in the future. Land for resale and long-term investments are examples of items that a local government could eventually turn into cash if the need arose. Cash on hand and accounts receivable are also included in this section of the consolidated statement of financial position.

Liabilities – are those items that a local government must expend cash resources to cover at some time in the future. Long-term debt is an element in the liabilities section of the consolidated statement of financial position that denotes borrowing for capital purposes (e.g. roads or sewer systems). Local governments frequently report long-term debt (liabilities) separately from short-term debt, such as a line of credit or bank overdraft (used for immediate cash needs). Long-term debt is normally a separate line item in the liabilities section of the consolidated statement of financial position. The notes section that accompanies a local government's annual financial statement may also provide detailed information on future long-term debt/liability repayment schedules.

Non-Financial Assets – include tangible capital assets (e.g. a fire truck) as well as inventory of supply and prepaid expenses. Tangible capital assets are included on the statement of financial position at their net book value – their actual cost less any accumulated amortization. Information about the original cost of the asset, and the amortization or use of the asset over time, is contained in the notes to the statement of financial position.

Accumulated Surplus – is the total amount of assets, both financial and non-financial, less any liabilities of the local government. The accumulated surplus is a key indicator of the financial resources a local government has available to provide future services to its citizens and meet its ongoing financial commitments. It consists of both cash and non-cash components.

The notes that accompany a local government's financial statements identify what portions of the accumulated surplus are:

- unrestricted (including cash, accounts receivable);
- restricted (cash that can only be used for a pre-determined purpose); and,
- equity in tangible capital assets.

Note: A net-debt position does not necessarily mean the local government is in financial difficulty. It simply means the local government has more liabilities than financial assets. However, a viable debt management plan needs to be in place to ensure that debt is sufficiently funded and that municipal services are not jeopardized.

City of Anywhere
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
As at December 31, 2010

	2010	2009
Financial Assets		
Cash and investments (Note 2)	\$ 7,369,624	\$ 6,658,836
Accounts receivable (Note 3)	4,473,644	1,943,094
MFA deposits (Note 4)	398,875	692,178
Business enterprise equity (Note 1)	3,200,000	3,000,000
Other financial assets	1,312,513	1,029,443
	16,754,656	13,323,551
Liabilities		
Accounts payable and accrued liabilities (Note 5)	1,542,473	1,433,667
Deferred revenue (Notes 6 & 7)	733,174	312,761
Development cost charges (Note 8)	1,776,478	68,380
Other restricted revenue	380,694	397,761
Capital leases (Note 9)	229,234	296,125
Long-term debt (Note 10)	13,488,377	11,868,790
Future Obligations (Note 11)	3,923,651	3,608,123
Other liabilities	159,628	125,195
	22,233,709	18,110,802
Net debt	(5,479,053)	(4,787,251)
Non-financial assets		
Tangible capital assets (Notes 1 & 12, Schedule 1)	50,770,697	48,818,283
Supply Inventory	112	222
Prepaid expenses	30	20
	50,770,839	48,818,525
Accumulated surplus (Note 13)	\$ 45,291,786	\$ 44,031,274

The accompanying notes and schedules are an integral part of these financial statements.

Consolidated Statement of Operations

The Consolidated Statement of Operations provides information about a local government's revenues, expenses and the year-end results (e.g. a surplus or deficit) for the reporting period. The statement of operations also provides detailed information regarding the specific transactions that have impacted the accumulated surplus over the course of the local government fiscal year. Non-cash items such as amortization expense and contributed assets are also commonly included in the consolidated statement of operations

There are three key elements of a consolidated statement of operations:

Revenue – is an accounting of all local government earnings in a given year. The main sources of local government revenue are property taxation and user fees collected for services such as garbage collection or recreation facilities. Government transfers are another revenue source – in the revenue section they include line items for federal, provincial or other regional government grants provided to a local government for operating and /or capital purposes.

Most revenue listings include a line item specifically for other revenues. This generally includes such revenues as contributed assets, which are normally tangible capital assets that have been donated or transferred to a local government from a developer or outside organization. Contributed assets are reported as revenue on the Statement of Operations because they create an expected future economic benefit, and result in an increase in a local government's year-end accumulated surplus. Although contributed assets are reported as revenue, they do not represent cash received by a local government.

Expenses – are monies spent during the year for any items that reduce the value of a local government's assets. Payment of salaries to staff, hydro, and mapping constitute expense, as does amortization.

Amortization – is a non-cash expense that represents the portion of the historical cost of a local government's tangible capital assets that is used up during the reporting period. Local governments may report the amortization expense as a separate line on their statement of operations or include the amortization expense in the costs of the specific service (e.g. drinking water or sewage disposal) provided by the local government.

Accumulated Surplus – is equal to the revenue less expenses for the year and is added to the amount from the previous year to equal the total included on the Statement of Financial Position. The accumulated surplus may increase significantly without a corresponding increase in a local government's financial assets. For example, a subdivision turned over to the local government by a developer would be recorded in the statement of operations as contributed asset revenue, which would in turn increase the accumulated surplus amount at year-end; however, there would be no change in the total financial assets held by the local government because it would instead be included in the value of the non-financial assets.

City of Anywhere
CONSOLIDATED STATEMENT OF OPERATIONS
for the year ended December 31, 2010

	2010 Budget	2010	2009
Revenue (Schedule 3)			
Property Taxes and grants in lieu (Note 15)	\$ 6,342,798	\$ 6,634,941	\$ 5,856,999
Sale of services (Note 16)	3,105,762	3,317,470	2,928,500
Government transfers (Note 17)	695,254	860,089	650,567
Investment income	385,645	447,996	424,596
Income from enterprises	190,000	200,000	(62,000)
Development cost charges (Note 8)	140,965	201,759	208,347
Other	23,129	255,373	261,954
	10,883,553	11,917,628	10,268,963
Expenses (Note 18, Schedule 3)			
General government	945,981	908,744	875,154
Protective services	3,962,546	3,812,040	3,512,961
Solid waste management and recycling	135,693	105,793	98,184
Public health	105,624	93,760	85,458
Planning and development	245,862	213,167	186,594
Transportation	602,845	509,990	450,685
Parks, recreation and culture	1,256,965	1,120,421	994,265
Water services	699,843	674,335	634,584
Sewer services	813,569	765,255	746,953
Debt financing	350,068	353,617	327,252
Amortization (Note 1, Schedule 1)	1,497,930	1,618,977	1,582,273
Loss from sale/write down of tangible capital assets (Schedule 1)	-	103,249	115,269
Other	266,627	377,768	185,295
	10,883,553	10,657,116	9,794,927
Annual surplus	-	1,260,512	474,036
Accumulated surplus at beginning of year	44,031,274	44,031,274	43,557,238
Accumulated surplus at end of year	\$ 44,031,274	\$ 45,291,786	\$ 44,031,274

The accompanying notes and schedules are an integral part of these financial statements.

Consolidated Statement of Changes in Net Debt

The Consolidated Statement of Changes in Net Debt illustrates the difference between a local government's annual surplus or deficit and the change in its net debt during the reporting period. The statement tracks local government expenditures used to acquire tangible capital assets (e.g. new vehicles) and pay for its inventories of supplies during the reporting period. The disposal of tangible capital assets, and the use of inventory and prepaid expenses (such as insurance paid at the beginning of the year and used during the year) are also captured in the statement of changes in net debt.

Some of the key elements of a consolidated statement of changes in net debt are:

Acquisition of tangible capital assets – the total funds spent by a local government acquiring tangible capital assets in the reporting year. Local governments generally use cash reserves, property taxes, long-term debt or government transfers to fund the purchase of tangible capital assets. The acquisition of tangible capital assets in the consolidated statement of changes in net debt also includes contributed asset values.

(Gain)/loss on sale of tangible capital assets – is the difference between the net book value of a tangible capital asset and the amount received from its disposal. The consolidated statement of changes in net debt shows a gain when a tangible capital asset is sold or is taken out of use and the proceeds are greater than the net book value of the asset. The consolidated statement of changes in net debt shows a loss when a tangible capital asset is liquidated and the proceeds are less than the net book value of the asset. Gains and losses associated with the sale of capital assets are also reported on the Statement of Operations – where a gain is reported as revenue and a loss is reported as an expense.

(Increase)/decrease in net debt – is the result of all the purchases and use of assets by a local government throughout the year, combined with the accumulated surplus from the consolidated statement of operations. An increase in a local government's net debt position is most likely the result of funding capital acquisitions with debt or with financial assets accumulated in prior years.

City of Anywhere
CONSOLIDATED STATEMENT OF CHANGES IN NET DEBT
for the year ended December 31, 2010

	2010 Budget	2010	2009
Annual surplus	-	\$ 1,260,512	\$ 474,036
Acquisition of tangible capital assets	(1,946,587)	(3,684,640)	(2,359,621)
Amortization of tangible capital assets	1,452,961	1,618,977	1,582,273
(Gain) / loss on sale of tangible capital assets	-	102,549	115,269
Proceeds on sale of tangible capital assets	-	10,000	35,000
Write downs of tangible capital assets	-	700	-
	(493,626)	(691,902)	(153,043)
Acquisition of supply inventory	(200) -		(329)
Acquisition of prepaid expense	(50)	(30)	(100)
Consumption of supply inventory	100	110	107
Use of prepaid expense	20	20	20
	(130)	100	(302)
(Increase)/decrease in net financial assets/net debt	(493,756)	(691,802)	(153,345)
Net financial assets/(net debt) at beginning of year	(4,787,251)	(4,787,251)	(4,633,906)
Net financial assets/(net debt) at end of year	\$ (5,281,007)	\$ (5,479,053)	\$ (4,787,251)

The accompanying notes and schedules are an integral part of these financial statements.

Consolidated Statement of Cash Flows

The Consolidated Statement of Cash Flows details the sources of cash and how the local government used that cash. The statement also provides details about any changes to a local government's cash and cash equivalents since the last reporting period, as well as detailed information about any significant cash transactions made by a local government not included in the Statement of Operations.

The Statement of Cash Flows tracks the change in the cash balance during a reporting period. It begins with the net results of local government operations – the annual surplus or deficit – and adds or subtracts transactions recorded in the other financial statements depending on whether or not they influence the cash balance. Items for which cash was paid reduce the cash balance; items that did not involve cash are added back to the surplus in order to accurately demonstrate the cash transactions.

There are four key elements of a consolidated statement of cash flows:

Operating Transactions – include revenues and expenses incurred during the day-to-day activities of a local government. Non-cash expenses are added back into the operations result. Amortization, a non-cash expense showing the use of a capital asset over time, is one example of a non-cash operating transaction. The amortization amount is added back into the operations result in order to determine the change in the local government's cash position.

Capital Transactions – are monies a local government expended on tangible capital assets as well as the amount a local government received from selling tangible capital assets during the reporting period.

Investing Transactions – include any increases or decreases in temporary or long-term investments such as interest earned on bonds owned by a local government. Legislation (both the *Local Government Act* and the *Community Charter*) restricts the types of investments (e.g. GICs, Bonds) local governments are permitted to make in order to limit the financial risk.

Financing Transactions – include funds received from long-term debt financing, as well as the amount of long-term debt principal repaid during the reporting period.

City of Anywhere
CONSOLIDATED STATEMENT OF CASH FLOWS
for the year ended December 31, 2010

(Indirect method)	2010	2009
Operating transactions:		
Annual surplus/(deficit)	\$ 1,260,512	\$ 474,036
Non-cash items:		
Amortization	1,618,977	1,582,273
Decrease in supply inventory	110	(222)
Increase in pre-paid expenses	(10)	(80)
(Gain)/Loss on the sale of tangible capital assets	102,549	115,269
Write down of tangible capital assets	700	-
Changes to financial assets/liabilities:		
Increase in accounts receivable	(2,530,550)	(1,596,324)
Decrease in MFA cash deposits	293,303	356,025
Increase in GBE investment	(200,000)	(100,000)
Increase in other financial assets	(283,070)	(255,568)
Increase in accounts payable	108,806	156,965
Increase in deferred revenue	420,413	126,953
Increase in development cost charges	1,708,098	29,563
Decrease in other restricted revenue	(17,067)	147,635
Increase in future obligations	315,528	329,654
Increase in other liabilities	34,433	25,914
Cash provided by operating transactions	2,832,732	1,392,093
Capital transactions:		
Acquisition of tangible capital assets	(3,684,640)	(2,359,621)
Proceeds from the sale of tangible capital assets	10,000	35,000
Cash applied to capital transactions	(3,674,640)	(2,324,621)
Investing transactions:		
Proceeds from sale of portfolio investments	-	-
Portfolio investments purchases	-	-
Other	-	-
Cash provided by (applied to) investing transactions	-	-
Financing transactions:		
Proceeds from debt issues	2,000,000	3,000,000
Debt repayment	(366,890)	(269,000)
Actuarial Adjustments	(80,414)	(68,596)
Cash applied to financing transactions	1,552,696	2,662,404
Increase in cash and cash equivalents	710,788	1,729,876
Cash and cash equivalents at beginning of year	6,658,836	4,928,960
Cash and cash equivalents at end of year	\$ 7,369,624	\$ 6,658,836

The accompanying notes and schedules are an integral part of these financial statements.

Frequently Asked Questions and Explanations

What statements comprise a local government's financial statements?

a) Consolidated Statement of Financial Position

The Consolidated Statement of Financial Position provides key details about a local government's assets, liabilities and any accumulated surplus for a given fiscal year. The statement provides the best indication whether or not a local government has the necessary assets to provide services to its residents in the future and meet its current financial commitments.

b) Consolidated Statement of Operations

The Consolidated Statement of Operations provides information about a local government's revenues, expenses and the year-end results (e.g. a surplus or deficit) for the reporting period. The consolidated statement of operations also provides detailed information regarding the specific transactions that have impacted the accumulated surplus over the course of the local government's fiscal year.

c) Consolidated Statement of Changes in Net Debt

The Consolidated Statement of Changes in Net Debt illustrates the difference between a local government's annual surplus or deficit and the change in its net debt during the reporting period. The statement tracks local government expenditures used to acquire tangible capital assets (e.g. new vehicles) and pay for its inventories of supplies during the reporting period.

d) Consolidated Statement of Cash Flows

The Consolidated Statement of Cash Flows details the sources of cash and how the local government used that cash. The statement also provides details about any changes to a local government's cash and cash equivalents since the last reporting period, as well as detailed information about any significant cash transactions made by a local government that are not included in the Statement of Operations.

How do the year-end results compare with the budget for the year (Did the local government budget well)?

The Statement of Operations and the Statement of Changes in Net Debt include the approved budget to compare with the actual results. The Annual surplus and the Accumulated surplus at year end on the Statement of Operations provide the end results.

The revenue and expense information in the Statement of Operations and the Statement of Changes in Net Debt provide additional information about how the actual year-end results compared to the budget. The Statement of Changes in Net Debt provides information regarding tangible capital assets, inventories and prepaid assets.

What is the local government's long-term debt position?

Long-term debt is generally incurred for capital purposes and is recorded separately on the Statement of Financial Position. The statement contains several notes to the financial statements that provide additional information regarding the long-term debt position. One of the notes identifies the type of debt (e.g. loan, debenture) and provides a schedule of principal and interest payments for each of the next five years. This schedule identifies the amount of principal and interest to be paid in the upcoming year. The principal paid in the next year is the current portion of the long-term debt.

The amount of money local governments in British Columbia may expend annually to service long-term debt is limited by legislation. This limit is updated annually and whenever a local government requests a new long-term debt servicing limit. The annual calculation is made with the information entered into the Local Government Data Entry (LGDE) system maintained by the Ministry, and shows how much capacity for future debt is available for each local government in the province.

What causes a change in net financial assets or net debt?

The Consolidated Statement of Changes in Net Debt reports how capital spending was funded – by increased revenues or increased debt. If no debt was incurred for capital spending, there would be no change in the net financial assets or net debt. If debt was incurred for capital spending, then the net financial assets would decrease or the net debt position would increase.

What is the Accumulated Surplus or Deficit?

The accumulated surplus position is the total amount by which local government assets exceed their liabilities. It is the indicator of a local government's economic resources available to provide future services. The accumulated surplus or deficit amount consists of cash and non-cash amounts and is separated into the following categories:

- **Unrestricted surplus/deficit** – this amount may include cash and other financial assets such as accounts receivable.
- **Restricted surplus (Reserve funds)** – the amount should be supported by cash. Reserve funds are established in legislation or by bylaw and segregate cash to be used for defined purposes.
- **Equity in tangible capital assets** – the value of tangible capital assets a local government owns. An example of this amount would be a fire truck purchased for \$500,000 (financed with a \$200,000 loan to be paid) that has been depreciated by \$50,000. The equity in the fire truck would be \$250,000 – which is the cost of the fire truck less the outstanding debt and accumulated amortization.

What created the change in the accumulated surplus/deficit?

The accumulated surplus may have increased significantly without any increase in financial assets. For example, an asset may have been contributed by a developer to the local government, increasing the accumulated surplus amount. The accumulated surplus or deficit amount can be separated into the following categories: unrestricted, restricted and equity in tangible capital assets. An accumulated surplus note to the financial statements can show the increase/decrease in each of these categories. Another note, 'Equity in Tangible Capital Assets', could provide summary information for the current and previous fiscal years.

What is restricted surplus?

Restricted surplus is one of the categories of the accumulated surplus/deficit amount. These restrictions identify funds for a specified future purpose and may, for example, result from agreements with third parties, or bylaws that designate these funds for a specific purpose. Sources of such funds include unused grants and funds set aside for specified future projects. The restricted surplus will normally consist of multiple funds and the 'accumulated surplus/deficit' note in the financial statements could provide the amount in each of these restricted surplus funds.

How much did the tangible capital assets depreciate this year?

This amount can be found under the heading of amortization. Tangible capital assets depreciate each year and the amount of this depreciation (referred to as 'amortization') is reported as an expense. Some local governments record this amortization expense as a separate line on the Statement of Operations or allocate the amortization expense to the appropriate service. The following statements will also report the total amortization expense for the year:

- Statement of Changes in Net Debt
- Statement of Cash Flow
- Schedule of Tangible Capital Assets

What is the condition of the tangible capital assets?

The Schedule of Tangible Capital Assets reports each major asset class, the total cost, accumulated amortization and net book value of tangible capital assets. The net book value of the total cost provides a broad indication of the remaining useful life of the tangible capital assets in each major asset class.

E.g.:	Vehicles	Cost	\$100,000
		Accumulated Amortization	\$90,000
		Net Book Value	\$10,000

In this example, the vehicles are nearing the end of their useful life and will likely need to be replaced in the near future.

Are there future planning or budgetary issues that should be addressed?

A review of the financial statements may identify some issues that need to be addressed to ensure the ongoing financial sustainability of the local government, including:

- net debt continues to increase;
- restricted surplus is not fully funded; e.g.: financial assets do not exist to support the restricted surplus;
- the short-term debt and the working capital position has been determined to be insufficient; or,
- net book value of the tangible capital assets is too low (e.g. the useful life is almost at the end).

Long-range planning for future budgets can positively address some or all of the above issues.

What are some potential 'red flags' in financial statements?

Potential "red flag" items might include:

- cash position has decreased significantly from the previous year;
- amount of cash and cash equivalents, including temporary investments, is less than the amount of restricted surplus identified in the Accumulated Surplus note to the financial statements;
- net financial assets reported on the Statement of Financial Position has significantly decreased or the net debt has significantly increased;
- net book value of the tangible capital assets is a low percentage of the total cost of the tangible capital assets; or,
- unrestricted portion of the accumulated surplus is in a deficit position.

What are the revenues from and costs of providing specific services?

For each specific service (such as water or sewer) provided by a local government to its citizens, the local government must generally ensure sufficient revenues are generated to cover all of the costs associated with providing the service. This includes a portion of the administrative costs of the local government in general, as well as the costs of operations, debt servicing and capital purchases.

A given service may be funded by parcel or assessment-based taxes, user fees, a combination of both, as well as other revenues. The revenues may be fixed or based on usage (such as for metered water).

Have there been any extraordinary or unusual financial transactions?

There may be significant financial transactions reported in the financial statements that have positively or negatively impacted the local government's financial position and 'bottom line'. The financial statements provide information for the previous fiscal year; comparing the current and prior year amounts is one way to determine if there were any extraordinary or unusual transactions.

Are there any contingencies that will have a future financial impact?

Contingencies are possibilities that may have future financial implications that are not recorded in the financial statements. These are shown in the notes to the financial statements, and those notes provide a brief explanation of the nature and potential future impact of each contingency.

What are the auditor's recommendations in the Management Letter?

The auditor is required to provide Council or the Board with a Management Letter at the conclusion of the annual audit. The Management letter is used to convey any matters the auditor identified during the financial statement audit to the local government. This letter normally identifies major concerns with recommendations to address those concerns.

How does a local government communicate the financial statement information to residents and businesses?

A summary of the audited financial results must be provided in a local government's annual report and be available for public viewing by June 30 each year. The complete set of the financial statements must also be made available upon request.

How do the funds in 'statutory reserves' fit into long range plans?

Funds may be set aside each year to pay for items Council or the Board is planning for the future. Statutory reserves are established to accumulate funds for these future projects and may include such items as development cost charges and capital renewal reserves. These funds are restricted and may only be used for specific future capital projects.

To assess the impact of a net debt position on the financial health of a local government, consider the following:

- *Is there a debt management plan in place?*
- *What is the term of the debt?*
- *What portion of the local government's liability servicing limit does the net debt represent?*
- *Are the local government's financial assets liquid and current?*
- *What portion, if any, of the local government's financial assets are restricted?*
- *What portion of the net debt is funded by the annual tax levy? By user fees?*
- *Will projected future revenues be sufficient to pay the net debt?*

If the answers to these questions are favourable, a local government is not likely to face financial difficulty in the near future.

Glossary of Terms

Amortization and Accumulated Amortization

Amortization is the annual allocation of a portion of the historical cost of a tangible capital asset held/owned by a local government as an expense over its useful life. Accumulated amortization is the total amortization of a tangible capital asset from the time the asset was placed into service until the date of the financial statement. The purpose of amortization is to show the decline in the asset's value as it ages or is used.

Construction in Progress

Items created in the fiscal year that have not been put into service; examples are engineered structures, buildings, and machinery and equipment that are not yet completely built.

Contributed Assets

Contributed assets are those assets transferred or donated to the local government by another entity. Contributed assets provide a future economic benefit to the receiving local government.

Deferred Revenue

Deferred revenue is income received by the local government that is not recorded as revenue until future conditions are met or events have taken place. Deferred revenue is held as a liability and may include items such as development cost charges and transfers for gas tax revenue.

Equity in Tangible Capital Assets

Equity in tangible capital assets is the net book value of recorded tangible capital assets less capital debt and related debt charges recoverable. Equity in tangible capital assets is that portion of the asset the local government actually owns - the remaining amount would be considered as debt.

Expenses

Expenses are the wide variety of costs incurred to run the local government, such as wages, materials, contracted services and interest on debt. Expenses do not include the purchase of tangible capital assets or payments of debt principal.

Financial Assets

Financial assets are the total cash and other resources (e.g. accounts receivable or investments) that could be converted into cash in the future.

Financial Plan

The financial plan – commonly referred to as a budget – must be adopted by the local government council or board annually. The budget must be adopted by bylaw and it must cover a minimum five-year period. Year one relates to the year in which it comes into force, years two through five are the following four years. Each year, the financial plan bylaw from the prior year remains in place until the financial plan bylaw for the current year is adopted.

Gain/Loss on the Sale of Tangible Capital Assets

Gain/Loss on the Sale of Tangible Capital Assets are the net proceeds resulting from the sale of a tangible capital asset where the proceeds are greater or less than the net book value of the asset.

Government Transfers

Government transfers are entitlements transferred to a local government under shared cost agreements, and grants from other levels of governments.

Liability Servicing Limit

A local government liability servicing limit is the total actual principal and interest charges on defined liabilities, plus the total of the average "implied" costs for all defined liabilities that are not yet recognized in the financial statements.

Local governments in British Columbia are generally restricted to a 25 percent liability servicing limit based on 25 percent of certain revenues.

Net Book Value of Tangible Capital Assets

The net book value of a local government's tangible capital assets is the total historical cost of the assets less the accumulated amortization and any write-downs of the tangible capital assets by the local government.

Net Financial Assets (Net Debt)

Net financial assets (net debt) is equal to the total financial assets held by a local government less the total liabilities owed by the local government.

Restricted Surplus

Restricted surplus is the amount resulting from excess revenues that have been internally designated for a specified future purpose, externally restricted, or formally designated.

Tangible Capital Asset

Tangible capital assets are physical assets such as land, buildings, infrastructure, and equipment that have a useful life of more than one year. They are used on a continuing basis and not for sale in the usual course of operations.

Write-downs of Tangible Capital Assets

Write-downs of tangible capital assets occur when there is a permanent decline in value of an asset held by a local government that is not reflected in the amortization of the asset. Write-offs are where the asset is no longer of value to a local government, but the item has a value left on the books that needs to be removed.

