Agenda - Council - July 21, 2004

Report - Alternate Service Delivery Committee - July 12, 2004

Item No. 2 Annual Selection Report 2004 - Glacial Sand and Gravel Special Operating Agency
File GL-5.6.1

COMMITTEE RECOMMENDATION:

On July 14, 2004, the Executive Policy Committee concurred in the recommendation of the Alternate Service Delivery Committee and submits the following to Council:

1. That the 2004 Selection Report for the Glacial Sand and Gravel Special Operating Agency (GSG), which contains Historical Financial Statements and the budget for Fiscal 2004, be approved as outlined in Appendix A to the report from the Director of Public Works dated July 7, 2004.

2. That the 2003 audited financial statements for Glacial Sand and Gravel Special Operating Agency, as outlined in Appendix B to the report from the Director of Public Works dated July 7, 2004, be received as information.

3. That the amendments to Glacial Sand and Gravel's Operating Charter, as adopted by Council on February 28, 2001, be approved as outlined on Appendix C to the report from the Director of Public Works dated July 7, 2004.

4. That the Proper Officers of the City be authorized to do all things necessary to implement the intent of the foregoing.

Report - Alternate Service Delivery Committee - July 14, 2004

DECISION MAKING HISTORY:

EXECUTIVE POLICY COMMITTEE RECOMMENDATION:

On July 14, 2004, the Executive Policy Committee concurred in the administrative recommendation and submitted the matter to Council.

COMMITTEE RECOMMENDATION:

On July 12, 2004, the Alternate Service Delivery Committee concurred in the administrative recommendation and submitted its recommendation to the Executive Policy Committee and Council.

ADMINISTRATIVE REPORT

Re: **ANNUAL SELECTION REPORT 2004: GLACIAL SAND AND GRAVEL SPECIAL OPERATING AGENCY**

For Submission To: **ALTERNATE SERVICE DELIVERY COMMITTEE**

Submitted By: **Bill Larkin, P. Eng. Director of Public Works**

Report Date: **July 7, 2004**

Recommendations:

1. That Council approve the 2004 Selection Report for the Glacial Sand and Gravel Special Operating Agency (GSG), which contains Historical Financial Statements and the budget for Fiscal 2004 as tabled in Appendix A.

2. That Council receive the 2003 audited financial statements for Glacial Sand and Gravel Special Operating Agency as information, in Appendix B.

3. That Council approve the amendments to Glacial Sand and Gravel's Operating Charter, that was adopted by Council on February 28, 2001, as tabled in Appendix C.

REPORT SUMMARY:

Key Issues:

- Critical elements of Glacial's original business plan have changed;
- Glacial's current model has not been and is not economically viable;
- Glacial must use 2004 to re-assess the economic merits of different business options going forward.
- The Operating Charter changes are consistent with the streamlining of reports proposed in the *ASD Policy and Process Review* and allow the Agency to operate in a more business-like manner.

IMPLICATIONS OF THE RECOMMENDATION(S):

General Implications:

X	None
	For the organization overall and/or other departments
	For the community and/or organizations external to the City

☐ Involves a multi-year phase in process

Comments:

Policy Implications:

	No
X	Yes

Comments: Amendments to the Agency's Operating Charter require Council approval.

Environmental Implications:

X	No
	Yes

Comments:

Human Resource Implications:

X	No
	Yes

Comments:

Financial Implications:

X	Within approved current and/or capital budget
	Current and/or capital budget adjustment needed

Comment: See attached financial projections.

REASON FOR THE REPORT:

The Glacial Sand and Gravel Operating Charter stipulates that a Selection Report (summary of the annual business plan) and an annual report will be submitted to Council each year.

HISTORY:

Glacial Sand and Gravel (GSG) was designated a Special Operating Agency (SOA) by Council effective January 1, 2001. Operating as a SOA, and adhering to business-like principles, was intended to produce the following benefits:

- Improve financial returns to the City over other alternative service delivery (ASD) options;
- Maintain control of the City of Winnipeg's sand and gravel resource assets; and
- Keep other ASD options open in the future.

The reduction in construction projects by City staff prior to GSG's consideration for Alternative Service Delivery resulted in declining aggregate material sales from Pine Ridge. The creation of GSG as a SOA provided an opportunity for the Agency to market value added processed products and raw pit materials to external organizations through various contractual and other arrangements. The creation of the SOA was intended to promote economies of scale that might ultimately lead to the acquisition of strategic high production, low cost per tonne, processing and handling equipment. The assumption was that operating as a high value-added producer of crushed gravel materials would maximize the economic returns from the assets.

DISCUSSION:

2003 was Glacial Sand and Gravel's third year of operation as a Special Operating Agency. 2003 was also the last year of the three year transition period as described in the Operating Charter. During this transition period, the Agency had a guaranteed market with the City for treated sand. In the new competitive environment, the Agency has to bid on all City contracts for aggregate products including treated sand.

The major component of the Agency's operations is the Pine Ridge Gravel Pit. This pit remains one of the last remaining high quality, clean, above-water sand and gravel deposits in close proximity to the City of Winnipeg. Glacial Sand and Gravel produces a variety of sand and gravel products at this location.

The second component of the Agency's operation is the Transcona Gravel Pit located off Provincial Hwy 207. This gravel pit is currently being mined on a per tonne royalty

basis by a private contractor. Limestone products are purchased from external vendors for sale to internal City of Winnipeg customers.

The hauling of all aggregate material is either carried out by the customers themselves or by the trucking firm under contract with the City of Winnipeg.

The original business plan envisioned GSG as a cost effective value added producer of crushed aggregate and building materials with significant sales of higher margin products to large multinational concrete producers and the City of Winnipeg. To realize the economic benefits of that operating model, significant capital expenditures for plant and equipment were anticipated in the early years and the perpetuation of highly profitable sales (especially treated winter sand) to the City of Winnipeg would be critical.

This current operating model has evolved with two fundamental deviations from the original business plan. These deviations include:

i. A much lower level and different type of capital investment in processing plant and equipment at GSG (from primarily high value added crushing to primarily low value added screening); and

ii. A departure from the assumption that GSG will continue to benefit from its formerly exclusive and profitable large volume sales to the City of Winnipeg.

Since its inception as an SOA in 2001, GSG has seen significant changes in key management and staff positions including the Chief Operating Officer, two Operations Coordinators and three Foremen. GSG has relied heavily on purchasing accounting and finance services from Public Works and has had four different primary accounting resources during this time.

The turnover of key people as described above has led to a certain amount of instability and lack of continuity in the strategic, operating and financial management at GSG. This management instability has certainly contributed to the difficulties faced by GSG to date and must be overcome to make GSG successful in the future.

Competitive Improvements

In adhering to business-like principles, the Agency continued to make the following competitive improvements:

- The ongoing introduction of computerized pit management systems that facilitate the inputting and analysis of data related to sales, production costing, and financial accountability;

- GSG continues to make very modest and prudent investment and upgrades to its existing equipment inventory. Some recent and anticipated examples include:

    - The recent acquisition and ongoing modification of a used triple deck screener to enhance productivity, safety, and efficiency;

    - The recent acquisition of a used 80 foot weigh scale with planned installation and associated scale house relocation and modifications to improve traffic flow, scale function and administrative support;

    - The recent acquisition of two previously rented material conveyors;

    - Office automation hardware and software upgrades to mitigate the risk of data loss from outdated systems, improve flexibility in work hours, and replace failing hardware;

GSG will conduct a detailed assessment of the merits of acquiring modern, high production crushing and material handling equipment as originally envisioned for the agency. This equipment remains fundamental to the value added material production operating model envisioned for GSG when it was originally formed.

Enhanced Pit Management

A move in the past two years by GSG to focus on screening materials and use contracted custom crushing services as needed has lead to a greater awareness of how to mine and screen materials effectively at Pine Ridge. GSG is now producing a higher proportion of products that occur naturally or require less processing than higher value added products made with high production crushing equipment.

GSG continues to make site modifications to improve resource extraction and processing efficiency, enhance equipment and truck traffic flow, promote pit safety and better serve customers.

GSG hopes to develop a comprehensive pit property and resource development plan over the next year as time and human resources allow. The property development plan will help GSG establish appropriate site development and resource access and extraction practices to ensure the responsible and profitable use of its various pit properties.

Raw Material Sales - Royalty Contracts

The SOA has entered into longer-term contracts, in accordance with the City's policies, to supply raw pit materials to individual customers for a royalty. These contractual arrangements supplement the revenue generated from GSG extracting and processing its raw materials itself.

Marketing

GSG is refining its pricing practices to be more competitive and structured by eliminating surcharges historically applied to certain materials, increasing prices based on current market conditions and competitor prices, and developing basic structured discounting practices. The completion of the product costing system will greatly enhance the Agency's ability to develop appropriate product pricing.

GSG continues to grow its organizational awareness of general marketing and sales concepts and practices in order to enhance its competitiveness and fulfill its mandate of acting in a business-like manner.

GSG hopes to develop its own comprehensive marketing strategy over the coming months as time and human resources allow. The marketing strategy will help GSG establish the appropriate product mix, pricing policies, geographic markets, and advertising and promotion practices.

Service Improvements

To increase customer service, the SOA will employ the following strategies:

- With the completion by mid 2004 of additional components for the computer based Weight Scale Management system, the SOA will be able to supply the customer with information such as:
    - amount of material stockpiled and available for immediate sale;
    - amount purchased and associated costs; and
    - history purchases including date, type of material and cost
- Increasing the gravel pit hours of operation to meet customer's material delivery needs.

Critical Success Factors

The following are GSG's critical success factors going forward in order of decreasing importance:

1. Replacing the substantial annual sales volumes and margins realized prior to December 31, 2003 under exclusive sales arrangements with the City of Winnipeg;
2. Establishment in 2005 of a new long-term raw material sales contract in the Transcona Pit to meet forecast sales as outlined in the financial projections;

3. Ability to take advantage of its highly desirable aggregate resources by supplying significant volumes of high value-added crushed gravel and aggregate products to the marketplace;
4. Overcoming the instability created by the loss of key staff and management over the past three years;
5. Effective development and performance management of GSG's human capital;
6. The ability to obtain cost effective and sensitive operating and administrative support services such as accounting, IT, HR, engineering, etc. through arrangements with both internal City of Winnipeg providers and external providers;
7. Completion of the product costing and inventory management components of our information systems;
8. Development and implementation of a comprehensive marketing strategy (i.e. fundamental direction for products, pricing, geographic markets, branding/advertising and promotion)
9. Development and implementation of pit/resource development plans for each GSG property;
10. Enhanced hours of operation; and
11. Effective quality control.

Financial Highlights

GSG has faced several critical financial issues under its current operating model that have detracted from its economic viability. These include:

- High cost structure relative to market competitors;
- Growing debt burden; and
- Lack of cash flow to finance necessary efficient, high volume production and handling equipment as originally anticipated;

Starting in 2004, following the three-year transition period, the new competitive environment facing GSG will only serve to exacerbate GSG's under performance in recent years.

The three issues listed above contributed to the following financial results for GSG in 2003. Earnings Before Taxes (EBT), which is an indication of the Agency's ability to generate operating income, underperformed budget by $139,000. Net income from 2003 underperformed budget projections by approximately $268,000. This was the result of higher than expected cost of sales and higher than expected expenses.

For 2004, revenues and expenditures are based on those experienced in 2002 and 2003 or on management's best estimates given recent performance and market conditions. The estimates are believed to be conservative. Expenditures will see equipment charges that reflect the 2003 purchase of the screening equipment.

Revenues will reflect the targeting of screened aggregate sales. Anticipated EBT for 2004 will be ($40,000) and Net Income is projected at ($28,000)

Historical and pro forma financial statements are attached which include a projected balance sheet, statement of earnings and retained earnings, and statement of cash flows (see Appendices A & B).

Performance Measurement

2003 was the third year of operation for Glacial Sand and Gravel as an SOA. The Agency continued to establish performance measurements for its operations. The table on the following page outlines the status of performance measures for four measurable performance goals.

GOAL	PERFORMANCE MEASUREMENT	MEASURE OF SUCCESSS/TARGET	STATUS (as of Dec. 31, 2003)
Financial	• Budgeted net income as per Selection Report projections	• To meet and/or exceed	• Underperformed
Operational	• Expand volume of materials produced at Pine Ridge location	• To meet and/or exceed	• Exceeded
	• Increase overall Agency volumes	• To meet and/or exceed	• Exceeded
	• Implement management information systems	• Systems installed	• Automated Weigh Scale system installed, inventory and costing systems development progressing
	• Meet and/or exceed productivity rates	• Initial benchmarking required	• To be developed
Customer Satisfaction	• Obtain customer satisfaction feedback	• Feedback and action taken	• To be implemented
Training and Development	• Implement a comprehensive training strategy	• Strategy implemented	• Strategy implemented
	• Provide cross-training opportunities	• Strategy implemented	• Cross training now provided on an ongoing basis
	• Obtain staff feedback	• Feedback and action taken	• To be implemented

Operating Charter Amendments

Currently, the SOAs produce annual business plans, quarterly reports and annual reports for Council. In order to ease the amount of reporting, it is recommended that there is no formal quarterly reporting requirement to Council. SOAs will still be held accountable through their annual business plan selection reports and their annual reports (including audited financial statements) that are submitted to Council. The purchasing policy delegation has been amended to reflect current business operations. These amendments to the Operating Charter is consistent with the streamlining of reports proposed in the ASD Policy and Process Review report adopted by Council on February 25, 2004 and allow the Agency to operate in a more business-like manner.

Conclusion

Critical elements of Glacial's original business plan have changed significantly since the SOA was formed. One of these elements was the ongoing deferral of the anticipated capital investment required for modern high output processing and handling equipment. This has made GSG a low value-added producer of material rather than a high value added producer. Initial assumptions about declining production costs and operating expenses have not been realized and are unlikely based on recent performance. Assumptions about GSG continuing to benefit from significant exclusive sales arrangements with the City of Winnipeg for several years after 2003 are highly uncertain due to the expiry of this arrangement this past December 31, 2003.

Glacial's financial future under the current operating model and new market realities is uncertain. For this reason, Glacial should operate on a status quo basis for 2004 while re-assessing the economic merits of different business options going forward. Unlike the Agency's previous selection reports that contained an annual budget and four-year projections, this report presents a one-year budget and historical financial information.

Advisory Board

The role of the Advisory Board is to provide advice on the Agency's strategic operations and on changes to its mandate, structure, business practices, and finances.

The Advisory Board is comprised of seven members; four City of Winnipeg employees, one CUPE Local 500 executive representative and two business representatives. It is anticipated over the coming year that the Board will replace business representative Mr. Bob Okabe who resigned from the Advisory Board in the spring of 2004.

Advisory Board Members:

Bill Larkin P. Eng.	Director of Public Works
W. Joe Funk P. Eng., MBA	Chief Operating Officer
Bruce McPhail P. Eng	CAO Representative

Jeff Laurent	Employee Representative
Jim Husiak, C.A.	CUPE Local 500 Representative
Bob Morris (Consultant)	Business Representative
Ed Bruning (I.H. Asper School of Business)	Business Representative

Appendix A: 3 Year Financial History and Projections

Glacial Sand and Gravel – Special Operating Agency

3 Year Financial History and Projections to

December 31, 2004

GLACIAL SAND & GRAVEL SOA

Balance Sheet
At December 31,

	2001 (Audited)	2002 (Audited)	2003 (Audited)	2004
Assets				
Current				
Cash	$ -	$ 100	$ 29,274	$ 100
Due from City of Winnipeg- General Revenue fund	147,623	-	-	-
Accounts receivable	271,273	245,849	291,746	308,711
Inventory	144,112	394,989	551,493	524,808
Income taxes recoverable	-	61,098	85,973	85,973
Prepaid expenses (Note 3)	83,461	-	-	-
Total Current Assets	646,469	702,036	958,487	919,592
Capital assets	3,965,162	4,279,083	4,527,392	4,382,574
	$ 4,611,631	$ 4,981,120	$ 5,485,879	$ 5,302,166
Liabilities				
Current				
Due to City of Winnipeg- General Revenue Fund	$ -	$ 203,669	$ 671,038	$ 506,533
Accounts payable and accrued liabilities	311,393	546,921	543,287	522,748
Income taxes payable	26,224	-	-	-
Rehabilitation payable	82,496	81,368	-	77,753
Vacation	30,360	39,641	41,843	39,843
Current portion of long term debt	50,885	84,936	151,405	150,444
Total Current Liabilities	501,358	956,535	1,407,572	1,297,321
Long Term				
Retirement allowance	82,000	100,000	84,000	102,000
Debt - City of Winnipeg	3,997,490	3,996,470	4,129,115	4,065,535
	4,079,490	4,096,470	4,213,115	4,167,535
RETAINED EARNINGS / (DEFICIT)	30,783	(71,885)	(134,808)	(162,690)
	$ 4,611,631	$ 4,981,120	$ 5,485,879	$ 5,302,166

GLACIAL SAND & GRAVEL SOA

Statement of Operations and Retained Earnings / (Deficit)
For the year ended December 31,

	2001 (Audited)	2002 (Audited)	2003 (Audited)	2004
Revenue	$ 2,084,869	$ 2,583,046	$ 2,958,505	$ 3,087,106
Cost of sales	1,061,870	1,872,044	2,134,100	2,141,150
Gross profit	1,022,999	711,002	824,405	945,956
Expenses				
Bank charges and interest expense (revenue)	1,836	1,109	-	37,977
Depreciation - property and equipment	27,462	49,628	91,132	100,683
Selling, general and administrative	683,374	594,593	581,217	572,958
Interest on long-term debt	263,320	260,121	280,182	274,721
	975,992	905,451	952,531	986,339
Earnings (loss) before income tax equivalents and government grant	**47,007**	**(194,449)**	**(128,127)**	**(40,384)**
Provision for income tax equivalents	(26,224)	86,840	53,597	-
Government grant	10,000	4,941	11,607	12,502
Net earnings (loss) for the year	**30,783**	**(102,668)**	**(62,923)**	**(27,882)**
RETAINED EARNINGS / (DEFICIT) BEGINNING OF YEAR	-	30,783	(71,885)	(134,808)
RETAINED EARNINGS / (DEFICIT) END OF YEAR	$ 30,783	$ (71,885)	$ (134,808)	$ (162,690)

GLACIAL SAND & GRAVEL SOA

STATEMENT OF CASH FLOWS
For the year ended December 31,

	2001	2002 (Actual)	2003 (Audited)	2004
CASH FLOWS FROM OPERATING ACTIVITIES				
Net income for the year	$ 30,783	$ (102,668)	$ (62,923)	$ (27,882)
Depreciation, depletion and amortization which do not require a cash outlay	125,673	109,628	173,079	196,818
Changes in non-working capital items:				
Decrease (increase) in accounts receivable	(271,273)	25,424	(45,897)	(16,965)
Increase in inventory	(144,112)	(250,877)	(156,504)	26,685
Increase (decrease) in income taxes recoverable	-	(61,098)	(24,875)	-
Decrease in prepaid expenses	(83,461)	83,461	-	-
Increase in accounts payable and accrued liabilities	311,393	235,529	(3,634)	(20,539)
Increase (decrease) in income taxes payable	26,224	(26,224)	-	-
Increase (decrease) in rehabilitation payable	82,496	(1,128)	(81,368)	77,753
Increase (decrease) in accrued vacation	30,360	9,281	2,202	(2,000)
	77,723	21,328	(199,920)	233,870
CASH FLOWS FROM INVESTING ACTIVITIES				
Purchase of fixed assets	(4,090,835)	(423,551)	(421,386)	(52,000)
CASH FLOWS FROM FINANCING ACTIVITIES				
Increase in retirement allowance	82,000	18,000	(16,000)	18,000
Increase (decrease) in debt- City of Winnipeg	4,048,375	33,031	199,114	(64,541)
	4,160,735	51,031	183,114	(46,541)
NET INCREASE (DECREASE) IN CASH	147,623	(351,192)	(438,192)	135,329
Cash (bank indebtedness) at beginning of year	-	147,623	(203,569)	(641,761)
CASH (BANK INDEBTEDNESS) AT THE END OF YEAR	$ 147,623	$ (203,569)	$ (641,761)	$ (506,432)

Notes to the Financial Projections

For Year ending December 31, 2004

1. Description of Business

On March 20, 1997, Council adopted a document entitled "Reshaping our Civic Government". The document identified the development of Special Operating Agencies (SOAs) as one of the five strategic initiatives needed to create a more affordable and fundamentally better Civic Government. On September 24, 1997, Council adopted the strategic direction with regard to SOAs identified in the report entitled "Special Operating Agencies Initiative." Consistent with the foregoing process, Equipment and Material Services of the Public Works Department prepared a report that outlined all options for alternate service delivery. This report identified the Special Operating Agency option as the most financially viable option. On February 23, 2000, Council directed Public Works to prepare a business plan based on the SOA recommendation. GSG commenced operations as an SOA on January 1, 2001.

The SOA deals in three primary products sold to the City of Winnipeg and other customers:

1.) Sand, gravel and aggregate products mined and processed at the Pine Ridge and Transcona pits;
2.) Crushed limestone products purchased and re-sold to City of Winnipeg departments and various external markets; and
3.) Salt treated sand that is produced for the City of Winnipeg and other users.

2. Accounting Principles

The projected financial statements have been prepared on the basis of Canadian generally accepted accounting principles. The projections include the following significant policies.

The preparation of periodic financial statements necessarily involves the use of estimates and approximations because the precise determination of financial data frequently depends on future events.

These financial statements have been prepared by management within reasonable limits of materiality and within the framework of accounting policies summarized below.

The financial statements have been prepared on the basis of Canadian generally accepted accounting principles and include the following significant accounting policies:

Inventory:

Inventory is recorded at the lower of cost and net realizable value.

Capital Assets:

Capital assets transferred from the City of Winnipeg on January 1, 2001 were recorded at their estimated value. Subsequent acquisitions are recorded at cost. Capital assets are amortized over the estimated useful life using the following rates and methods:

Machinery	10 years	Straight Line

Buildings	4 – 5%	Declining Balance
Office Equipment	20%	Declining Balance
Computer Equipment	30%	Declining Balance

The depletion of the gravel pit is recorded at a rate of 20 cents per tonne of aggregate inventory extracted on an annual basis.

Revenue Recognition:

Revenue is recognized upon delivery of products.

Financial Instruments:

Financial instruments include accounts receivable, income taxes recoverable, due to City of Winnipeg - General Revenue Fund, accounts payable and accrued liabilities, and long-term debt. Unless otherwise stated, it is management's opinion that the Agency is not exposed to significant interest, currency or credit risks arising from these financial instruments. The book value of the Agency's financial assets and liabilities approximates their fair value.

3. Fixed Assets, Plant & Equipment

The agency acquired certain of the equipment and structures owned by the former Primary Materials Branch. In addition, land in the amount of $15,720 has been included at book value. The Agency plans to evaluate the costs and benefits of acquiring additional strategic plant and equipment such as a modern crusher, wheel loader, overland conveyors, etc. vs. renting. Previous capital expenditures are being financed via long-term debt through Fleet Management Agency, repayable over a 5 year period at an interest rate of 6.5% (the City of Winnipeg long term borrowing rate).

The City and the SOA determined, and mutually agreed, that the value of the Pine Ridge Pit at December 31, 2001 was $3,800,000, and this value was placed on the SOA balance sheet along with a similar amount in long-term debt. Interest is paid at a rate of 6.5%. Principal will be repaid at a mutually agreed upon date in the future, consistent with Council decision in this regard.

4. Financial Projections

This financial projection is an estimate of the financial position, results of operations, and change in cash flow for the operation of GSG Special Operating Agency, using management’s assumptions that reflect the Agency’s planned course of action for the year ending December 31, 2004.

These projections are based on the SOA operating as a self-contained business unit, including all costs required to support its operations. Cost categories considered and included are: human resources, operations and maintenance, facilities, capital expenditures and associated operating or term debt, overhead and one-time conversion costs. These costs represent a full costing model.

Management's judgment has been used in the assumptions and the most probable set of economic conditions, together with the hypotheses stated in note 5 below. The hypotheses are consistent with the purpose of the information, but are not necessarily the most probable in management's judgment. Since assumptions inevitably will not materialize and unanticipated events and circumstances may occur subsequent to the date of this projection, the actual results achieved during the projected period will vary from the projections and the deviations may be material.

5. Hypotheses

The financial projection has been prepared based on the following hypotheses:

a) That the SOA will be allowed to purchase any support services from the City or external providers required to sustain ongoing operations.

b) As the SOA continues as part of the municipal government structure, the entity is not subjected to corporate income taxation. However, in order to approximate a business model, the financial projections of the entity reflect a provision for income tax equivalents at a rate of 40%, payable to the City of Winnipeg. In addition, future income tax assets which represent the carry forward of unused tax losses have been included for illustrative purposes where there is a reasonable belief by management that these tax assets can be utilized in the future. These are utilized in future years to offset income tax equivalents payable. No future income tax liability has been recorded as the assumption has been made that depreciation/depletion for accounting purposes approximates capital cost allowance for taxation purposes.

c) That the City of Winnipeg will continue to extend an operating loan and provide long term lending sufficient for the Agency to commence operations with interest charged at 6.5%.

d) According to the annual business plan, a portion of any positive earnings will be reinvested into the SOA.

e) The Council approval of GSG's Selection Report.

f) Funding for necessary strategic plant and equipment acquisitions must come from GSG cash flows.

6. Assumptions - Revenue

Approximate sale tonnages and dollars are based on recent experience and anticipated market conditions going forward. All information is reflected FOB pit or quarry.

Sales	2004 Tonnes	2004 Dollars
Pine Ridge	356,000	$1,573,000
Transcona	125,000	$265,000
Limestone	30,000	$178,000

Treated Sand (from Pine Ridge**)**	54,000	$551,000
Total	565,000	$2,567,000

7. Assumptions - Expenses

Note: Unless separately disclosed, all non-material expenditures have assumed a 2% inflationary increase each year.

a) **Salaries and employee benefits**

The SOA expects to operate with the following staff levels over the next five years:

- WAPSO Exempt 1
- WAPSO 1
- CUPE 9
- CUPE (summer students) 3

Employee benefits are estimated to be 16% of total gross salaries.

b) **Audit Fees**
The SOA expects to pay $6,500 annually towards audit fees.

c) **Automobile Allowances**
Automobile allowance expenses of approximately $8,000 are expected to be incurred by GSG management.

d) **Advertising/Sales Promotion**
The SOA expects to spend $7,500 for advertising and promotion annually.

e) **Depreciation**
Depreciation is based on rates identified in Note 2.

f) **Depletion**
Pit depletion will be charged at 20¢ /tonne for the Pine Ridge and Transcona pits.

l) **Administrative Charges**
The SOA expects to purchase administrative services from the Public Works Department. Included in these costs are fees for financial, human resources, and information technology totaling $25,000 annually.

m) **Interest**
Interest will be paid at an annual rate of 6.5% for its long-term debt and operating line of credit.

n) **Other Governmental Charges**
Payments for the Provincial Rehabilitation Levy of 10¢/tonne and the Rural Municipality of Springfield's Aggregate Mining Levy and Road Maintenance Levy of 6.8¢/tonne will be expensed on an annual basis. The Provincial Rehabilitation Levy extinguishes the SOA from further site restoration obligations.

8. Assumptions – Assets and Liabilities

a) **Cash on hand**
Petty cash of $100 will be available for incidental expenditures.

b) **Accounts Receivable**
Accounts receivable have been calculated on the basis of approximately 1 month of sales being outstanding at year end. As a result, 10% of revenues have been shown as the receivable balance. The SOA has budgeted $20,000 annually to cover outstanding accounts where payment is not ready.

c) **Aggregate Inventory**
The agency has purchased the gravel pit asset at a value of $3,800,000. It is being financed as long-term debt from the City of Winnipeg at an annual rate of 6.5%.

d) **Property and equipment**
The agency will purchase in accordance with Note 3.

e) **Accounts payable and accrued liabilities**
Accounts payable will be paid on the basis of 30 day terms and it has been assumed that accounts payable will include approximately 5% of eligible expenses.

f) **Retirement allowance and vacation liability**
At the time of agency inception, a liability was determined that would extinguish the amounts entitled to employees of the agency upon retirement.

g) **Due to City of Winnipeg**
The agency will require short-term financing in the form of an operating line of credit from the City of Winnipeg from the Idea Bank. Interest will be paid to the Idea Bank at a rate of 6.5%.

h) **Long-term debt**
Debt for property and equipment purchases is obtained from either Fleet Management Agency or the City of Winnipeg. Debt taken for the purchase of the gravel pit in the amount of $3,800,000 will incur interest charges at 6.5% which will be payable to the Idea Bank.

9. Long-term Debt

$3,800,000 in debt for the Pine Ridge Pit has no fixed term of repayment (see Note 3) Long term debt at December 31 of the following years consists of the following:

	2004
Debt (interest rate 6.5%)	$ 4,216,000
Less: current portion	$ 150,000
Long-term portion	$ 4,056,000

Appendix B: Audited Financial Statements

Glacial Sand and Gravel – Special Operating Agency

Audited Financial Statements at

December 31, 2003

Financial Statements

The City of Winnipeg Glacial Sand and Gravel – Special Operating Agency

December 31, 2003

AUDITORS' REPORT

To the Mayor and Members of City Council
The City of Winnipeg

We have audited the statement of financial position of **The City of Winnipeg Glacial Sand and Gravel – Special Operating Agency** as at December 31, 2003 and the statements of operations and retained earnings and cash flows for the year then ended. These financial statements are the responsibility of the Agency's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of **The City of Winnipeg Glacial Sand and Gravel – Special Operating Agency** as at December 31, 2003 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Winnipeg, Canada,
April 23, 2004

Chartered Accountants

THE CITY OF WINNIPEG
GLACIAL SAND AND GRAVEL - SPECIAL OPERATING AGENCY

STATEMENT OF FINANCIAL POSITION

As at December 31
(in thousands of dollars)

	2003	2002
ASSETS		
Current		
Cash	**$ 29**	$ -
Accounts receivable (Note 3)	**292**	246
Income taxes recoverable (Note 4)	**86**	61
Inventory	**551**	395
	958	702
Capital assets (Note 5)	**4,527**	4,279
	$ 5,485	$ 4,981
LIABILITIES		
Current		
Due to City of Winnipeg - General Revenue Fund (Note 6)	**$ 671**	$ 204
Accounts payable and accrued liabilities	**543**	547
Rehabilitation payable (Note 7)	**-**	81
Vacation payable (Note 8a)	**42**	40
Current portion of long-term debt (Note 9)	**151**	85
	1,407	957
Retirement allowance (Note 8b)	**84**	100
Long-term debt (Note 9)	**4,129**	3,996
	5,620	5,053
CAPITAL DEFICIENCY		
Deficit	**(135)**	(72)
	$ 5,485	$ 4,981

See accompanying notes to the financial statements

THE CITY OF WINNIPEG
GLACIAL SAND AND GRAVEL - SPECIAL OPERATING AGENCY

STATEMENT OF OPERATIONS AND DEFICIT

For the year ended December 31
(in thousands of dollars)

	2003	2002
REVENUES		
Sales of goods and services (Note 10)	**$ 2,959**	$ 2,583
EXPENSES		
Administrative services (Note 10)	**72**	123
Amortization and depletion	**173**	109
Interest on long-term debt (Note 9)	**280**	261
Material, parts and supplies	**516**	474
Salaries and benefits	**634**	598
Services	**1,400**	1,208
	3,075	2,773
Net loss before income taxes	**(116)**	(190)
Income tax recovery (Note 4)	**53**	87
Net loss for the year	**(63)**	(103)
(DEFICIT)/RETAINED EARNINGS, BEGINNING OF YEAR	**(72)**	31
DEFICIT END OF YEAR	**$ (135)**	$ (72)

See accompanying notes to the financial statements

THE CITY OF WINNIPEG
GLACIAL SAND AND GRAVEL - SPECIAL OPERATING AGENCY

STATEMENT OF CASH FLOWS

For the year ended December 31
(in thousands of dollars)

NET INFLOW (OUTFLOW) OF CASH RELATED TO THE FOLLOWING ACTIVITIES:

	2003	2002
OPERATING		
Net loss for the year	**$ (63)**	$ (103)
Non-cash items related to operations		
Amortization and depletion	**173**	109
Retirement allowance	**(16)**	18
Working capital from operations	**94**	24
Net change in working capital	**(310)**	14
	(216)	38
FINANCING		
Due to City of Winnipeg - General Revenue Fund	**467**	352
Repayment of long-term debt	**(85)**	(90)
Proceeds of issuance of long-term debt	**284**	123
	666	385
INVESTING		
Purchase of capital assets	**(421)**	(423)
INCREASE IN CASH POSITION	**29**	-
CASH POSITION, BEGINNING OF YEAR	**-**	-
CASH POSITION, END OF YEAR	**$ 29**	$ -

See accompanying notes to the financial statements

THE CITY OF WINNIPEG
GLACIAL SAND AND GRAVEL - SPECIAL OPERATING AGENCY

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2003
(in thousands of dollars, except as noted)

1. Description of Business

Glacial Sand and Gravel - Special Operating Agency ("Agency") commenced operations on January 1, 2001. Since the inception, sales of gravel pit aggregate, limestone, and treated sand are realized from both The City of Winnipeg and private industry customers.

2. Summary of Significant Accounting Policies

The preparation of periodic financial statements necessarily involves the use of estimates and approximations because the precise determination of financial data frequently depends on future events. These financial statements have been prepared by management within reasonable limits of materiality and within the framework of accounting policies summarized below.

The financial statements have been prepared on the basis of Canadian generally accepted accounting principles and include the following significant accounting policies:

Inventory

Inventory is recorded at the lower of cost and net realizable value.

Capital assets

Capital assets transferred from the City of Winnipeg on January 1, 2001 were recorded at their estimated value. Subsequent acquisitions are recorded at cost. Capital assets are amortized over the estimated useful life using the following rates and methods:

Machinery	10 years	Straight-line
Buildings	4-5%	Declining balance
Office equipment	20%	Declining balance
Computer equipment	30%	Declining balance

The depletion of the gravel pit is recorded at a rate of 20 cents per tonne of aggregate inventory extracted on an annual basis.

Revenue Recognition

Revenue is recognized upon delivery of products.

Financial Instruments

Financial instruments include accounts receivable, income taxes recoverable, due to City of Winnipeg - General Revenue Fund, accounts payable and accrued liabilities, and long-term debt. Unless otherwise stated, it is management's opinion that the Agency is not exposed to significant interest, currency or credit risks arising from these financial instruments.
The book value of the Agency's financial assets and liabilities approximates their fair value.

3. Accounts Receivable

	2003	2002
Trade accounts receivable	**$ 326**	$ 269
Government of Canada	**-**	2
Allowance for doubtful accounts	**(34)**	(25)
	$ 292	$ 246

4. Income Tax Equivalency

As part of the municipal government, the Agency is not subject to corporate income taxes. However, in order to approximate a business model, the operation of the Agency is assessed with an income tax equivalency charge/recovery of 46% which is payable to (recoverable from) The City of Winnipeg. Amounts paid are to be directed to infrastructure renewal in the City of Winnipeg.

5. Capital Assets

	Cost	**Accumulated Amortization/ Depletion**	**Net Book Value 2003**	Net Book Value 2002
Gravel pit	**$ 3,800**	**$ 240**	**$ 3,560**	$ 3,642
Machinery	**980**	**145**	**835**	511
Building under capital lease	**51**	**3**	**48**	50
Computer equipment	**53**	**17**	**36**	26
Land clearing	**28**	**-**	**28**	28
Building	**19**	**2**	**17**	18
Office equipment	**4**	**1**	**3**	4
	$ 4,935	**$ 408**	**$ 4,527**	$ 4,279

6. Due to City of Winnipeg - General Revenue Fund

The City of Winnipeg operates a centralized treasury function with a single operating bank account in the General Revenue Fund. Consequently, the Agency does not have a bank account. Cash transactions are credited or charged to the "Due (to)/from" account. Interest is credited or charged based on the City's average short-term earnings (cost of funds) on the single bank account.

The Agency has negotiated an operating line of credit of up to $400 thousand from The City of Winnipeg - Idea Bank Reserve, at a rate of 6.5%.

7. Rehabilitation Payable

The Agency is required to pay rehabilitation fees for future restoration of the land and surrounding infrastructure when the gravel pit has been depleted. These fees are assessed as follows:

Province of Manitoba - rehabilitation fee of 10 cents per tonne sold
RM of Springfield - mining fee of 4.4 cents per tonne sold
RM of Springfield - road maintenance levy of 2.4 cents per tonne sold

8. Employee Benefits

a) Vacation

The Agency's employees accrue vacation credits, which together with unused holidays from previous years generally become a charge to operations in the year they are earned.

b) Retirement allowance

Under various union agreements, unused sick leave credits accumulate and employees with specified minimum service requirements become entitled to a cash payment upon retirement, death or termination of service under certain conditions (excluding resignation). An actuarial valuation has estimated the retirement allowance liability at December 31, 2003 at $84 thousand (2002 - $100 thousand).

c) Pension

The Agency's employees are eligible for pensions under the Winnipeg Civic Employees' Benefits Program. The Plan is a defined benefit plan. The City of Winnipeg allocates its pension costs to various departments. During the year, $31 thousand (2002 - $32 thousand) of pension costs were allocated to the Agency. An actuarial valuation for the Winnipeg Civic Employees' Benefits Program was made as of January 1, 2003 and has an actuarial surplus.

9. Long-Term Debt

	2003	2002
City of Winnipeg - Equipment and Materials Services:		
Equipment replacement loan, interest at 6.5%, payment of $2 thousand monthly, due September 2005	**$ -**	$ 65
Equipment financing program loan, interest at 6.5%, payment of $5 hundred monthly, due December 2005	**11**	16
Equipment loan, interest at 6.5%, payment of $5 thousand monthly, due December 2005	**109**	158
Gravel pit loan, interest at 6.5%, no repayment schedule	**3,800**	3,800
City of Winnipeg - Fleet Management - Special Operating Agency		
Equipment replacement loan, interest at 6.5%, payment of $2 thousand monthly, due September 2005	**42**	-
Equipment loan, interest at 6.5%, payment of $6.5 thousand monthly, due February 2008	**284**	-
Capital lease obligation, interest at 7.6%, monthly payments of $0.9 thousand, due April 2008	**34**	42
	4,280	4,081
Current portion of long-term debt	**(151)**	(85)
	$ 4,129	$ 3,996

9. Long-Term Debt (continued)

a) Principal repayments due within the next five years are as follows:

2004	$ 151
2005	155
2006	78
2007	83
2008	13
Thereafter	3,860
	4,280

b) Interest on the equipment loans during the year was $33 thousand (2002 - $14 thousand) and has been paid to The City of Winnipeg - Equipment and Material Services and Fleet Management - Special Operating Agency; and

The interest payable on the gravel pit loan during the year of $247 thousand (2002 - $247 thousand) is to be directed to infrastructure renewal in the City of Winnipeg.

c) Cash paid for interest during the year was $33 thousand (2002 - $14 thousand).

10. Related Party Transactions

Included in the Agency's revenues/expenses are the following transactions, which occurred in the normal course of operations and are recorded at the exchange amount:

a) Sales of goods and services of $925 thousand (2002 - $972 thousand) to The City of Winnipeg for treated sand; and

b) General government charges in the amount of $26 thousand (2002 - $58 thousand) to The City of Winnipeg - General Revenue Fund which represents the estimated share of The City of Winnipeg's general expenses applicable to the Agency.

11. Comparative Figures

Certain comparative figures have been reclassified to conform to the current year's financial statement presentation.

Appendix C: Recommended Operating Charter Amendments

Glacial Sand and Gravel – Special Operating Agency

Amendments to Glacial Sand and Gravel's Operating Charter:

OPERATING CHARTER	CURRENT	RECOMMENDED
Section 3: Accountability Framework *Council Responsibility*	After a start up period no longer than six months, Council receives summary quarterly and annual reports as information to assess Agency performance.	Recommended language: *Council receives annual reports as information to asses Agency's performance and policy outcomes.*
Chief Operating Officer Responsibility	The COO provides the Advisory Board with agency plans, summary quarterly reports, annual reports, charter revisions, and other proposals and information required from time to time for effective management and accountability.	Recommended language: *The COO provides the Advisory Board with annual business plans, annual reports, charter revisions, and other proposals and information required from time to time for effective management and accountability.*
Advisory Board	The Advisory Board reviews and comments on the Agency's proposed agency plans, summary quarterly and annual reports, and charter revisions.	Recommended language: *The Advisory Board reviews and comments on the Agency's proposed annual business plans, annual reports, and charter revisions.*
Section 4: Planning and Reporting Framework *Quarterly Reports*	Interim reports on the Agency's financial position and progress against key objectives and performance targets will be prepared each quarter. After an appropriate startup period, quarterly reports will be forwarded in summary form to Council as information.	Delete sub-section that refers to *Quarterly Reports*.
Appendix 1: Delegations and Exemptions	d) By approval of this Charter, the Agency has the authority to exercise choice in the purchase of services either internal or external to the City of Winnipeg, provided that standards of consistency and connectivity for communications and reporting are maintained. In the interest of business efficiency, the Agency has the authority to sole source the purchase and acquisition of granular materials and transportation of the same.	Recommended language: *The Agency must comply with the City of Winnipeg's Materials Management Policy, with the exceptions that the Chief Operating Officer has the delegated authority to:* *a. approve single source purchases, in accordance with B4 of the Materials Management Policy, not contravening the Agreement on International Trade for goods and services, with the exception that the COO has the delegated authority to*

		purchase granular materials and transportation of the same, and not to exceed $100,000; *b. award contracts pursuant to the Materials Management Policy and within the jurisdiction of the Agency consistent with that of the Director of Public Works, for contracts with consideration not to exceed $ 150,000; and* *c. award contracts where the contract does not create an absolute commitment for funds not yet approved by Council, consideration for the contract does not exceed $150,000, and the contract does not exceed five years.*

Financial Impact Statement

Date:

Project Name:

First Year of Program:

	0	1	2	3	4
Capital					
Capital Expenditures Required	$ -	$ -	$ -	$ -	$ -
Less: Existing Budgeted Costs	-	-	-	-	-
Additional Capital Budget Required	$ -	$ -	$ -	$ -	$ -
Funding Sources:					
Debt - Internal	$ -	$ -	$ -	$ -	$ -
External	-	-	-	-	-
Grants (Identify)	-	-	-	-	-
Reserves, Equity, Surplus, Other	-	-	-	-	-
Total Funding	$ -	$ -	$ -	$ -	$ -
Total Additional Capital Budget Required	$ -				
Total Additional Debt Required	$ -				
Current Expenditures/Revenues					
Direct Costs	$ -	$ -	$ -	$ -	$ -
Less: Incremental Revenue/Recovery	-	-	-	-	-
Net Cost/(Benefit)	$ -	$ -	$ -	$ -	$ -
Less: Existing Budget Amounts	-	-	-	-	-
Net Budget Adjustment Required	$ -	$ -	$ -	$ -	$ -

Additional Comments:

"Original signed by Darcy Stewart, CA"
Manager of Finance and Administration

Approved by Divisional Accounting Technician:
Approved by Divisional Accountant Trainee: ☒

This Report Submitted by:

Department:	Public Works Department
Division:	Glacial Sand & Gravel SOA
Prepared by:	W. Joe Funk P. Eng., MBA Phone No: 986-5335
File name:	Glacial 2004 Selection Report (July 7 Final)