

CORPORATION OF HAMILTON

Annual Financial Statements
(With Independent Auditor's Report Thereon)

December 31, 2017

The accompanying report of KPMG Audit Limited ("KPMG") is for the sole and exclusive use of the Corporation of Hamilton (the "Corporation"). No person, other than the Corporation, is authorized to rely upon the report of KPMG unless KPMG expressly so authorizes. Furthermore, the report of KPMG is as of June 7, 2018 and KPMG has carried out no procedures of any nature subsequent to that date which in any way extends that date.



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INDEPENDENT AUDITOR'S REPORT

To the Members of The Corporation of Hamilton

Opinion

We have audited the financial statements of The Corporation of Hamilton (the "Corporation"), which comprise the statement of financial position as at December 31, 2017, the statements of operations, changes in accumulated surplus, net debt and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2017, and its financial performance and its cash flows for the year then ended in accordance with public sector accounting standards generally accepted in Bermuda and Canada.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("ISA"). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Corporation in accordance with the ethical requirements that are relevant to our audit of the financial statements in Bermuda, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Material uncertainties related to going concern

The accompanying financial statements have been prepared assuming that the Corporation will continue as a going concern. We draw attention to Notes 2 and 14 to the financial statements which describe the potential impact on the Corporation of ongoing legal proceedings against the Corporation and amendments to Municipalities Act 1923. These conditions indicate the existence of a material uncertainties that may cast significant doubt about the Corporation's ability to continue as a going concern. Management's plans in regard to these conditions are described in Note 2. The financial statements do not include any adjustments that might result from the outcome of these material uncertainties. Our opinion is not modified in respect of these matters.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

In preparing the financial statements, management is responsible for assessing the Corporation's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Corporation or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Corporation's financial reporting process.



Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISA will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISA, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Corporation's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Corporation to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

KPMG Audit Limited

Chartered Professional Accountants
Hamilton Bermuda
June 7, 2018

CORPORATION OF HAMILTON

Statement of Financial Position

December 31, 2017

(Expressed in Bermuda Dollars)

	<u>2017</u>	<u>2016</u>
Financial assets		
Cash and cash equivalents	\$ 5,321,998	\$ 4,984,764
Accounts receivable, net (Notes 3 and 7)	1,383,591	1,598,481
Recoverable costs	<u>86,025</u>	<u>93,028</u>
Total financial assets	<u>6,791,614</u>	<u>6,676,273</u>
Liabilities		
Accounts payable and accrued liabilities (Notes 4 and 11)	4,878,315	10,415,015
Long-term loans (Notes 6 and 11)	5,594,498	6,613,599
Pension plans and other post retirement benefits (Note 7)	<u>1,129,910</u>	<u>1,174,852</u>
Total liabilities	<u>11,602,723</u>	<u>18,203,466</u>
Net debt	<u>(4,811,109)</u>	<u>(11,527,193)</u>
Non-financial assets		
Tangible capital assets, net (Note 5)	65,893,082	64,140,723
Inventory of materials and supplies	215,872	456,608
Prepaid expenses	<u>48,691</u>	<u>43,172</u>
Total non-financial assets	<u>66,157,645</u>	<u>64,640,503</u>
Accumulated surplus	<u>\$ 61,346,536</u>	<u>\$ 53,113,310</u>

The accompanying notes are an integral part of the financial statements.

Signed on behalf of the Corporation of Hamilton:


_____ Charles R Gosling, Mayor


_____ Tanya Iris, Acting Secretary and Treasurer

CORPORATION OF HAMILTON

Statement of Operations

For the Year Ended December 31, 2017

(Expressed in Bermuda Dollars)

	Budget <u>2017</u>	Actual <u>2017</u>	Actual <u>2016</u>
Revenue			
Property taxes	\$ 8,662,600	\$ 8,658,613	\$ 8,588,847
Goods wharfage	6,087,000	6,894,793	6,322,083
Car parking fees	3,255,068	3,065,915	2,882,818
Sewage disposal contracts	2,284,546	2,286,314	2,284,546
Rents from properties	934,162	1,003,709	941,678
Other permit and license fees	380,652	570,785	435,120
Ships wharfage	365,000	420,601	358,940
Dock charges	120,000	286,920	188,424
City Hall rents	90,000	102,015	100,533
Miscellaneous	44,360	40,206	49,946
Interest	<u>8,580</u>	<u>21,684</u>	<u>12,012</u>
Total revenue (Note 12)	<u>22,231,968</u>	<u>23,351,555</u>	<u>22,164,947</u>
Expenditures			
Administrative and general expenses	9,356,968	8,770,895	8,880,196
Sanitation services	3,360,124	3,467,121	3,526,558
Street operations and maintenance	2,796,912	3,183,899	2,934,794
Parks and gardens maintenance	1,754,965	1,747,097	1,478,677
Wharf operations and maintenance	1,323,888	1,323,683	1,252,660
Works depot expenses	1,205,370	1,038,195	1,092,795
Sewerage maintenance and operating	639,083	535,447	517,933
Interest and finance charges	667,211	534,078	552,461
City Hall maintenance	744,748	331,124	474,898
Car parks expenses	164,913	217,944	200,328
Provision for doubtful accounts	168,000	168,214	163,315
Property maintenance	<u>200,000</u>	<u>71,582</u>	<u>171,669</u>
Total expenditures (Notes 9 and 12)	<u>22,382,182</u>	<u>21,389,279</u>	<u>21,246,284</u>
Excess (shortfall) of revenue over expenditures before undernoted item	(150,214)	1,962,276	918,663
Derecognition of liability on guarantee (Note 14)	–	–	18,752,548
Derecognition of fire service accrual (Note 4)	<u>–</u>	<u>6,270,950</u>	<u>–</u>
Excess (shortfall) of revenue over expenditures	<u>\$ (150,214)</u>	<u>\$ 8,233,226</u>	<u>\$ 19,671,211</u>

The accompanying notes are an integral part of the financial statements.

CORPORATION OF HAMILTON

Statement of Changes in Accumulated Surplus

For the Year Ended December 31, 2017

(Expressed in Bermuda Dollars)

	<u>2017</u>	<u>2016</u>
Accumulated surplus, beginning of year	\$ 53,113,310	\$ 33,442,099
Excess of revenue over expenditures	<u>8,233,226</u>	<u>19,671,211</u>
Accumulated surplus, end of year	<u>\$ 61,346,536</u>	<u>\$ 53,113,310</u>

The accompanying notes are an integral part of the financial statements.

CORPORATION OF HAMILTON

Statement of Changes in Net Debt

For the Year Ended December 31, 2017

(Expressed in Bermuda Dollars)

	<u>2017</u>	<u>2016</u>
Excess of revenue over expenditures	\$ 8,233,226	\$ 19,671,211
Acquisition of tangible capital assets, net	(3,438,741)	(1,831,761)
Amortization of tangible capital assets, net	1,686,382	1,646,563
Acquisition of inventory	(973,924)	(637,277)
Consumption of inventory	1,214,660	742,274
Acquisition of prepaid expenses	(438,158)	(435,678)
Consumption of prepaid expenses	<u>432,639</u>	<u>435,760</u>
Decrease in net debt	6,716,084	19,591,092
Net debt, beginning of year	<u>(11,527,193)</u>	<u>(31,118,285)</u>
Net debt, end of year	\$ <u>(4,811,109)</u>	\$ <u>(11,527,193)</u>

The accompanying notes are an integral part of the financial statements.

CORPORATION OF HAMILTON

Statement of Cash Flows

For the Year Ended December 31, 2017

(Expressed in Bermuda Dollars)

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities		
Excess of revenue over expenditures	\$ 8,233,226	\$ 19,671,211
Adjustments for non-cash items		
Amortization of tangible capital assets, net	1,686,382	1,646,563
Derecognition of liability on guarantee	-	(18,000,000)
Derecognition of fire service accrual	(6,270,950)	-
Changes in non-cash working capital balances:		
Decrease in accounts receivable	214,890	654,360
Decrease (increase) in recoverable costs	7,003	(76,156)
Increase in accounts payable and accrued liabilities	734,250	419,070
Decrease in pension plans and other post retirement benefits	(44,942)	(51,929)
Decrease in inventory of materials and supplies	240,736	104,997
(Increase) decrease in prepaid expenses	<u>(5,519)</u>	<u>82</u>
Net cash from operating activities	<u>4,795,076</u>	<u>4,368,198</u>
Cash flows from investing activities		
Acquisition of tangible capital assets, net	<u>(3,438,741)</u>	<u>(1,831,761)</u>
Net cash used in investing activities	<u>(3,438,741)</u>	<u>(1,831,761)</u>
Cash flows from financing activities		
Bank loan repayments	<u>(1,019,101)</u>	<u>(736,580)</u>
Net cash used in financing activities	<u>(1,019,101)</u>	<u>(736,580)</u>
Net increase in cash and cash equivalents	337,234	1,799,857
Cash and cash equivalents, beginning of year	<u>4,984,764</u>	<u>3,184,907</u>
Cash and cash equivalents, end of year	<u>\$ 5,321,998</u>	<u>\$ 4,984,764</u>
Supplemental cash flow disclosure:		
Interest paid for the year (Note 6)	<u>\$ 449,418</u>	<u>\$ 469,800</u>
Interest received for the year	<u>\$ 21,684</u>	<u>\$ 12,012</u>

The accompanying notes are an integral part of the financial statements.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

1. **General**

The Corporation of Hamilton (the “Corporation”) is responsible for the provision of certain municipal services within the boundaries of the City of Hamilton (the “City”) in accordance with the Municipalities Act 1923 (the “Act”). The principal sources of revenue include property taxes, goods wharfage, sewage disposal and car parking fees. The various expenditures are controlled by committees established for sanitation, sewerage, wharfs, parks, properties, streets, finance and City Hall.

2. **Significant accounting policies**

These financial statements have been prepared in accordance with accounting principles generally accepted in Bermuda and Canada as provided by the Public Sector Accounting Board (“PSAB”) of the Chartered Professional Accountants of Canada (“CPA Canada”).

The preparation of financial statements in accordance with public sector accounting standards generally accepted in Bermuda and Canada requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenditures for the year. Actual amounts could differ from those estimates. Significant areas requiring the use of management estimates relate to the measurement of pension plans and other post-retirement benefits, the amortization and potential impairment of tangible capital assets, the recoverability of accounts receivable and the estimate of accrued and contingent liabilities and contingent assets.

Going concern

Mexico Infrastructure Finance LLC (“MIF”) obtained a summary judgment in the amount of US\$18 million against the Corporation on May 27, 2015, (see Note 14) under a guarantee given by the Corporation for the loan to Par-la-Ville Hotel and Residences, Ltd (“PHRL”). MIF sought enforcement of the \$18 million judgment debt against the Corporation and PHRL that raised substantial doubt about the Corporation’s ability to continue as a going concern, if forced to repay this debt out of current income. The Corporation considered several options including the sale of assets and debt financing or a combination of both and finally settled on obtaining a loan from a local bank (refer to Note 14 for an update on the loan and guarantee position). The Corporation was also working with the Bermuda Government to find ways to increase revenue in order to repay the debt. In November 2016, the Corporation sought and won a judgment in the Supreme Court to have the May 27, 2015 summary judgment set aside (see Note 14). The judge ruled that MIF cannot recover the loan from the Corporation by enforcing the guarantee which the court has ruled to be ultra vires. In May 2017, the Court of Appeal upheld the Supreme Court ruling that the guarantee was ultra vires. The Corporation is, therefore, not liable for the guarantee. In June 2017 MIF served notice of its application for leave to appeal to the Privy Council against the Court of Appeal’s ultra vires judgement. A court date has been set for October 2018 (see Note 14).

The judgment does not prevent MIF from using other causes of action to recover the funds. MIF started additional legal proceedings against the Corporation in the Supreme Court of the State of New York on this matter (see Note 13c). The outcome of these legal proceedings are not yet known. The ability of the Corporation to repay any debt against the Corporation arising from such action out of current income will still lead to a going concern uncertainty as all attempts to raise sufficient revenue through legislation have failed. However, the Corporation has reviewed its cash flow position for at least but not limited to the next 12 months and has determined there will be sufficient cash and revenues to continue as a going concern.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

2. Significant accounting policies (continued)

As explained in Note 15, in March 2018 the Government of Bermuda passed the Municipalities Amendment Act which announced changes to the Act. These changes could have an impact on the Corporation's ability to operate as a going concern. The Government of Bermuda also announced its intention to undertake consultation with the Corporation, residents, ratepayers and the general public to determine the most appropriate method to strengthen and modernize municipal governance for the benefit of Bermuda. Any further amendments to the Act or municipal reform may call into question the Corporation's ability to continue as a going concern.

These financial statements have been prepared on a going concern basis which assumes that the Corporation will continue to operate for the foreseeable future. This is dependent on the following assumptions:

- there being no further reforms to the Act impacting on the Corporation's ability to continue to operate;
- the ability of the Corporation to meet its liabilities as they fall due and operate in line with its latest forecasts and projections; and
- The future outcome of any legal proceedings by MIF against the Corporation.

These financial statements do not include any adjustments to the carrying values of the assets and liabilities if the Corporation is unable to continue as a going concern. Such adjustments could be material.

The following are the significant accounting policies adopted by the Corporation:

(a) Revenues

Revenues are recorded on the accruals basis and recognized when earned. Amounts that have been received in advance of services being rendered are recorded as deferred revenue until the Corporation discharges the obligations that led to the collection of funds.

(b) Budget information

Budget information approved by the Corporation and the Minister responsible for the Municipalities in December 2016 is presented using a basis consistent with that used for the actual results.

(c) Expenditures

Expenditures are recorded on the accruals basis in the period in which the goods or services are acquired or a liability is incurred.

(d) Non-financial assets

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

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

2. Significant accounting policies (continued)

(d) Non-financial assets (continued)

(i) Tangible capital assets

Tangible capital assets are recorded at cost which includes amounts that are directly attributable to the acquisition, construction, development or betterment of the asset. The costs, less residual values, of the tangible capital assets, excluding land, are amortized on a straight-line basis over their estimated useful lives as follows:

<u>Assets</u>	<u>Useful life – Years</u>
Betterments	50
Buildings	40 – 100
Fixed plant and equipment	3 – 50
Mobile plant and equipment	8 – 15
Roads	100
Sewer lines	40 – 100
Wharfs	75

Annual amortization is charged in the year of acquisition and in the year of disposal. Land is not amortized. Assets under construction are not amortized until the asset is available for productive use.

Subsequent expenditures incurred after the assets have been put into operation, such as repairs and maintenance and overhaul costs, are charged to the statement of operations in the period the costs are incurred. However, expenditures that result in an increase in the future economic benefit in excess of the originally assessed standard of performance of the existing asset are capitalized as an additional cost of tangible capital assets. When assets are sold or retired, their cost, accumulated amortization and accumulated impairment losses are eliminated from the financial statements and any resulting gain or loss is included in the statement of operations of such period.

Contributions of tangible capital assets

Tangible capital assets received as contributions are recorded at their fair values at the date of receipt and also are recorded as revenue.

Works of art and cultural and heritage assets

Works of art and cultural and heritage assets are not recorded as tangible capital assets in these financial statements.

Methods used for determining the cost of each major category of tangible capital assets

The financial information recorded includes the actual or estimated historical cost of the tangible capital assets. When historical cost records were not available, other methods were used to estimate the costs and accumulated amortization of the assets. The Corporation applied a consistent method of estimating the replacement or reproduction cost of the tangible capital assets for which it did not have historical cost records, except in circumstances where it could be demonstrated that a different method would provide a more accurate estimate of the cost of a particular type of tangible capital asset. After defining replacement or reproduction cost, the Canada Non-residential Building Construction Price Index formulated by Statistics Canada was used as a resource for determining appropriate indices in order to deflate the replacement or reproduction cost to an estimated historical cost at the year of acquisition.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

2. Significant accounting policies (continued)

(d) Non-financial assets (continued)

(ii) Inventories

Inventories are comprised of supplies and materials to be used to maintain properties and other assets of the Corporation and are valued at the lower of average cost and net realizable value.

(iii) Impairment of non-financial assets

At each statement of financial position date, tangible capital assets, net, and other long-lived assets are reviewed for impairment whenever events or circumstances indicate that the carrying amount of an asset exceeds its recoverable amount. The excess is recognized as impairment loss in the statement of operations and the assets or cash generating units are written down to their recoverable amounts. The recoverable amount is the higher of an asset's net selling price and value in use. The net selling price is the amount obtainable from the sale of an asset in an arm's length transaction, while value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the asset. Recoverable amounts are estimated for individual assets or, if it is not possible, for the cash-generating unit to which the assets belong.

(iii) Impairment of non-financial assets (continued)

Impairment losses recognized in prior years are reversed when there is an indication that the impairment losses recognized for the asset no longer exist or have decreased. The reversal is recorded as income in the statement of operations. However, the increased carrying amount of an asset due to the reversal of an impairment loss is recognized only to the extent that it does not exceed the carrying amount that would have been determined had impairment loss not been recognized for that asset in the prior periods.

(e) Pension plans and other post retirement benefits

The Corporation sponsors a defined contribution pension plan and a deferred annuity plan, together covering all eligible employees. The cost of both of these plans is expensed as earned by the employees. The Corporation makes monthly contributions in accordance with the plan agreements to the employees' individual accounts, which are administered by an insurance company pursuant to and in accordance with the National Pension Scheme (Occupational Pensions) Act 1998 and applicable amendments thereto and regulations.

The Corporation sponsors a defined benefit plan for post-retirement medical healthcare benefits of its eligible former employees. The Corporation closed this plan for new members with effect from August 2008. The Corporation pays 50% of the total premiums due to the insurer with the remainder being assumed by the insured. The cost of accrued retirement benefit obligations is actuarially determined using the projected unit credit method and represents the Corporation's share of the present value of future premiums for former employees over their expected lives. Actuarial gains and losses on the accrued retirement benefit obligation arise from differences between actual and expected experience and from changes to actuarial assumptions used to determine the accrued benefit obligation. Actuarial gains and losses on the accrued benefit obligation are recognized over the average remaining life of the former employees.

The expenses related to these plans are included in wages, salaries and benefits (Notes 7, 9 and 12).

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

2. Significant accounting policies (continued)

(f) Cash and cash equivalents

Cash includes cash on hand and in banks. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less from dates of acquisition and that are subject to an insignificant risk of changes in value.

(g) Receivables

Receivables are recognized and carried at their nominal values or invoice amounts as reduced by appropriate allowances for doubtful accounts.

Bad debts, if any, are written off during the year.

(h) Allowance for doubtful accounts

The Corporation provides an allowance for doubtful accounts when there is evidence that the Corporation will not be able to collect all amounts due according to the original terms of receivables. The amount of provision is equal to the estimated collection losses based on past collection experience and management's review of the current status of the long-outstanding receivables.

(i) Payables and provisions

Payables are stated at their nominal values.

The Corporation recognizes a provision if a present obligation has arisen as a result of a past event, payment is probable, and the amount can be measured reliably. The amount recognized is the best estimate of the expenditure required to settle the present obligation at the statement of financial position date, that is, the amount the Corporation would rationally pay to settle the obligation to a third party.

(j) Leases

The Corporation as lessor

Costs, including amortization, incurred in earning lease income are recognized as an expense. Lease income (excluding receipts for services provided such as insurance and maintenance) is recognized on a straight-line basis over the lease term. Lease income is recorded in rents from properties in the statement of operations.

(k) Related parties

Parties are considered related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Corporation members, officers, shareholders, associates or companies and other related interests that directly or indirectly control or are controlled by or under common control are considered related parties. The changes to the Municipalities Act in March 2018 creates a related party relationship between the Corporation and the Government of Bermuda (see Note 15). The full impact will not be known until the conclusion of the consultation period.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

2. Significant accounting policies (continued)

(l) Segment disclosures

A segment is defined as a distinguishable activity or group of activities of a government for which it is appropriate to separately report financial information to achieve the objectives of the standard. The Corporation has adopted PSAB Section PS 2700 *Segment disclosures* and has provided definitions of segments used by the Corporation as well as presented financial information in segmented format in Note 12.

(m) Future accounting standards

Financial instruments

PSAB issued Section PS 3450 *Financial Instruments* in March 2011. This section proposes reporting on the nature and extent of risks associated with financial instruments held and issued by an entity. Financial instruments which are quoted in an active market will need to apply fair value measurement (e.g. equity investments or derivatives). All other non-derivative financial instruments will be measured at cost or amortized cost unless the entity elects to apply the fair value option. To support meaningful budget to actual comparisons, when fair value measurement is applied, the presentation of surplus/deficit will need to be reported both excluding and including any re-measurement gains or losses. Early adoption is permitted. This standard is effective for the Corporation's December 31, 2019 financial statements and management does not anticipate a significant impact as a result of adoption.

Financial statement presentation

In conjunction with Section PS 3450, PSAB also issued, Section PS 1201 which replaces the existing Section PS 1200, *Financial Statement Presentation*, and includes a new statement of re-measurement gains and losses. The new statement will report unrealized gains and losses associated with financial instruments in the fair value category, exchange gains and losses associated with monetary assets and liabilities denominated in a foreign currency, amounts reclassified to the statement of operations upon derecognition, and other comprehensive income reported when a public sector entity includes the results of its government business enterprises and partnerships in the financial statements. Early adoption is permitted. This standard is effective for the Corporation's December 31, 2019 financial statements and management does not anticipate a significant impact as a result of adoption.

3. Accounts receivable

Accounts receivable are shown net of an allowance for doubtful accounts of \$1,118,506 (2016 - \$1,008,162). The Traffic Offences Procedure Act (the "Act") 1974 was effective from June 1, 2017. Section 18A of the Act states "The penalty for a parking offence committed within a municipal area shall accrue to the revenues of the Corporation of Hamilton. Included in accounts receivable is an accrual of \$127,525 (2016 - \$nil) for parking ticket revenue for the period June to December 2017.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

4. Due to the Government of Bermuda and accounts payable and accrued liabilities

Due to the Government of Bermuda

The Hamilton Fire Service was originally set up by the Corporation and then transferred to the Government of Bermuda. At that time, the Corporation agreed to assist with paying a share of the fire service costs. The last payment was made in 2008 as a formal agreement had never been signed for this arrangement and the peppercorn lease as described below had expired. However, based on confirmations received from the Government of Bermuda, the Corporation continued to accrue for potential expenses payable until October 2017. Included in accounts payable and accrued liabilities as at December 31, 2016, is an amount of \$6,270,950 which may have been due to the Government of Bermuda that represents fire service expense in relation to the operations of the Hamilton Fire Service.

The Corporation also expected to receive payment of \$4,550,000 from the Government of Bermuda related to rental revenue for the fire service property for the period to December 31, 2016. The original lease for the property which was for a period of 25 years and an annual rent of only \$1 ended in 2008 and a new lease agreement has never been finalized. However, as no amounts were received from the Government in relation to this rent, no amount was recorded that related to this revenue or contingent asset in the Corporation's financial statements.

In October 2017, the Government of Bermuda agreed to write off the receivable of \$6,270,950 from the Corporation and the Corporation also agreed to write off rental income of \$4,550,000 due from the Government with the expectation that the outstanding tipping fees will also be waived. The derecognition of the fire service accrual of \$6,270,950 is included in the statement of operations for the year ended December 31, 2017.

Tipping fees of \$2,998,683 (2016 - \$2,336,626) due to the Government of Bermuda have been accrued as at December 31, 2017 and are included in vendor accounts payable.

Accounts payable and accrued liabilities is comprised of:

	<u>2017</u>	<u>2016</u>
Vendor accounts payable	\$ 3,959,891	\$ 3,153,091
Accrued liabilities	468,073	424,373
Employee benefits payable	192,281	167,853
Interest payable	107,522	121,276
Unearned revenue	106,383	217,289
Other payables	44,165	60,183
Due to Government of Bermuda for fire services	<u>—</u>	<u>6,270,950</u>
	<u>\$ 4,878,315</u>	<u>\$ 10,415,015</u>

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

5. Tangible capital assets, net

	<u>2016</u>	<u>Additions</u>	<u>Disposals</u>	<u>Transfers</u>	<u>2017</u>
Cost					
Land	\$ 12,052,112	\$ –	\$ –	\$ –	\$ 12,052,112
Betterments	2,853,068	–	–	78,691	2,931,759
Buildings	41,088,693	–	–	116,634	41,205,327
Fixed plant and equipment	10,580,421	18,921	(51)	631,220	11,230,511
Mobile plant and equipment	3,127,426	814	–	560,336	3,688,576
Roads	869,191	–	–	–	869,191
Sewer lines	3,528,144	–	–	895,074	4,423,218
Wharf	20,452,524	–	(8,623)	242,004	20,685,905
Assets under construction	<u>2,110,436</u>	<u>3,427,680</u>	<u>–</u>	<u>(2,523,959)</u>	<u>3,014,157</u>
Total	\$ 96,662,015	\$ 3,447,415	\$ (8,674)	\$ –	\$ 100,100,756
	<u> </u>				
			<u>2016</u>	<u>Amortization expense</u>	<u>2017</u>
Accumulated amortization					
Betterments			\$ 243,803	\$ 64,899	\$ 308,702
Buildings			11,454,362	576,324	12,030,686
Fixed plant and equipment			5,459,815	484,296	5,944,111
Mobile plant and equipment			2,228,029	181,502	2,409,531
Roads			413,890	7,834	421,724
Sewer lines			1,416,448	91,619	1,508,067
Wharf			<u>11,304,945</u>	<u>279,908</u>	<u>11,584,853</u>
			<u>\$ 32,521,292</u>	<u>\$ 1,686,382</u>	<u>\$ 34,207,674</u>
			<u> </u>	<u> </u>	<u> </u>
			<u>2016</u>		<u>2017</u>
Net book value					
Land			\$ 12,052,112		\$ 12,052,112
Betterments			2,609,265		2,623,057
Buildings			29,634,331		29,174,641
Fixed plant and equipment			5,120,606		5,286,400
Mobile plant and equipment			899,397		1,279,045
Roads			455,301		447,467
Sewer lines			2,111,696		2,915,151
Wharf			9,147,579		9,101,052
Assets under construction			<u>2,110,436</u>		<u>3,014,157</u>
			<u>\$ 64,140,723</u>		<u>\$ 65,893,082</u>
			<u> </u>		<u> </u>

Assets under construction are not subject to depreciation until placed into service.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

6. Long-term loans

The Corporation has the following long-term loans outstanding:

	<u>2017</u>	<u>2016</u>
Clarien Bank Limited ("Clarien Bank")	\$ 5,594,498	\$ 6,310,159
Bank of N.T. Butterfield & Son Limited ("Butterfield Bank")	<u>—</u>	<u>303,440</u>
	<u>\$ 5,594,498</u>	<u>\$ 6,613,599</u>

On April 19, 2010, the Corporation obtained an \$11 million loan facility to finance the construction of its Works Depot on Laffan Street, Hamilton, from Clarien Bank of which \$10.6 million was drawn down in 2010 and 2011. As security for the loan, Clarien Bank holds a registered mortgage over the property.

The loan is to be repaid over 15 years from the date it was granted at an interest rate of 1.75% above Clarien Bank's Bermuda dollar base rate. The effective interest rate is 6.0% per annum at December 31, 2017 (2016 - 5.75%).

Monthly payments of interest were required during the construction phase. Commencing December 31, 2011, the loan is being repaid in annual installments of blended interest and principal \$1,068,075.

In June 2012, the Corporation obtained a loan from Butterfield Bank in the amount of \$500,000 to purchase and upgrade land on the corner of Court and Dundonald Streets. The loan carries an interest rate of 4.75% and repayment over 10 years. As security for the loan, Butterfield Bank holds a registered mortgage over the property. This loan was fully repaid during the year.

The future minimum principal payments are as follows:

	<u>Total</u>
2018	\$ 740,515
2019	780,341
2020	822,309
2021	866,534
2022 and thereafter	<u>2,384,799</u>
Total	<u>\$ 5,594,498</u>

Interest paid during the year was \$449,418 (2016 - \$469,800).

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

7. Pension plans and other post-retirement benefits

As described in Note 2(e), the Corporation sponsors a defined contribution pension plan and a deferred annuity plan, together covering all eligible employees. Contributions to these plans by employees are at the rate of 5% of remuneration, which is matched by the Corporation for the defined contribution plan. The Corporation's contributions under the deferred annuity plan are equal to the amount required to pay up the cost of the annuities applicable to the current year of employment.

Pension and deferred annuity contributions for the year are as follows:

	<u>2017</u>	<u>2016</u>
Corporation's contributions	\$ 527,891	\$ 469,754
Employee contributions	\$ 364,153	\$ 359,768

Included in accounts receivable is a defined contribution pension surplus balance of \$nil (2016 - \$168,315), which represents the Corporation's contributions for former employees whose employment ceased prior to the end of the vesting period. The pension surplus can be offset against future pension contributions payable by the Corporation.

The Corporation also sponsors a defined benefit plan for post-retirement medical healthcare benefits to eligible former employees. This plan was valued by qualified actuaries as at December 31, 2017. Information about this plan is as follows:

	<u>2017</u>	<u>2016</u>
Accrued benefit obligation		
Balance, beginning of year	\$ 1,456,655	\$ 1,515,893
Interest cost	79,221	75,389
Benefits paid	(157,786)	(159,831)
Actuarial (gain) loss	(144,853)	25,204
Balance, end of year	\$ 1,233,237	\$ 1,456,655
Plan assets		
Fair value, beginning of year	\$ -	\$ -
Employer contributions	157,786	159,831
Benefits paid	(157,786)	(159,831)
Fair value, end of year	\$ -	\$ -
Funded status		
Accrued benefit obligation	\$ 1,233,237	\$ 1,456,655
Unamortized actuarial loss	(103,327)	(281,803)
Retirement benefit liability	\$ 1,129,910	\$ 1,174,852

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

7. **Pension plans and other post-retirement benefits** (continued)

The significant assumptions used are as follows:

	<u>2017</u>	<u>2016</u>
Accrued benefit obligation:		
Discount rate	5.75%	5.75%
Benefits cost for the year:		
Discount rate	5.75%	5.75%
Healthcare cost trend rates:		
Rates in years 2018 to 2019	6.0%	6.5%
Ultimate rate in 2019 and beyond	6.0%	7.0%

Increasing or decreasing the assumed healthcare cost trend rates by one percentage point would have the following effects for 2017:

	<u>Increase</u>	<u>Decrease</u>
Total of service cost and interest cost	\$ 5,240	\$ (4,774)
Accrued benefit obligation	\$ 72,241	\$ (66,141)

The elements of the Corporation's retirement healthcare benefit costs recognized during the year are as follows:

	<u>2017</u>	<u>2016</u>
Interest cost	\$ 79,221	\$ 75,389
Actuarial (gain) loss	<u>(144,853)</u>	<u>25,204</u>
Element of retirement benefit costs before adjustments	(65,632)	100,593
Adjustments to recognize the long-term nature of retirement benefit costs:		
Difference between recognized and actual actuarial loss	<u>178,476</u>	<u>7,309</u>
Employee future benefit cost recognized	<u>\$ 112,844</u>	<u>\$ 107,902</u>

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

8. Reserves

The Corporation may appropriate reserves for specific purposes. Reserves consist of the following funds included within accumulated surplus:

	<u>2017</u>	<u>2016</u>
CB Tucker fund	\$ 32,500	\$ 32,500

9. Expenditures by object

	<u>2017</u>	<u>2016</u>
Wages, salaries and benefits	\$ 10,031,166	\$ 9,633,667
Contract services	7,302,505	7,566,382
Supplies and materials	1,835,148	1,847,211
Amortization of tangible capital assets, net	1,686,382	1,646,563
Interest and finance	<u>534,078</u>	<u>552,461</u>
	\$ 21,389,279	\$ 21,246,284

10. Capital commitments

The Corporation has contractual commitments for capital expenditures as at December 31, 2017, in the amount of \$215,771 (2016 - \$216,753), which will be paid for in 2018.

11. Financial instruments

The estimated fair values of the Corporation's cash and cash equivalents, accounts receivable, recoverable costs and accounts payable approximate their respective carrying values due to their short-term nature. The estimated fair value of the long-term loans approximates carrying value as the loans attracts market rates of interest. The Corporation is not exposed to significant currency risk from its financial instruments as these are denominated in either Bermuda dollars or United States dollars.

(a) *Interest rate risk*

The Corporation is exposed to interest rate fluctuations with respect to the long-term loans and retirement benefit liability which bears interest at floating rates as disclosed in Notes 6 and 7, respectively. Management does not believe that the impact of interest rate fluctuations will be significant.

(b) *Credit risk*

The Corporation's cash and cash equivalents are held with three financial institutions based in Bermuda. The Corporation has accounts receivable from a wide range of individuals, businesses, and government organizations. Management actively monitors outstanding accounts receivable. The Corporation's maximum exposure to credit risk is represented by the carrying amount of its financial assets in the statement of financial position.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

11. Financial instruments (continued)

(c) Liquidity risk

Liquidity risk is the risk that the Corporation will encounter, difficulties meeting its financial obligations as they become due. The table below summarizes the Corporations contractual undiscounted cash flows. Balances due within twelve months are met within the Corporation's normal thirty-day cycle of disbursements.

	<u>Total</u>	<u>0-3 months</u>	<u>4-12 months</u>	<u>Greater than 1 year</u>
December 31, 2017				
Accounts payable	4,658,372	4,461,790	196,582	–
Long-term loans	5,702,020	15,729	1,115,262	4,571,029
December 31, 2016				
Accounts payable	10,076,450	9,789,046	287,404	–
Long-term loans	6,734,875	15,729	1,115,262	5,603,884

12. Segmented reporting

The Corporation provides a range of services to both residents and businesses within the boundaries of the City. Certain services such as connection to the City sewer lines are available to persons/businesses outside the City boundaries on a fee basis. Most revenue lines have been allocated directly to the relevant segment. However, taxation has been split equally between Governance and Civic Services, Sanitation and Sewer, and Public Works and Planning in order to defray some of the costs of providing these services. From April 1, 2014, the Government of Bermuda returned the right of the Corporation to charge goods wharfage on imported goods. For segmented disclosure purposes, these services are grouped and reported under service areas/departments that are responsible for providing such services. They are as follows:

Governance and Civic Services

City Hall provides for the Mayoral and Council functions, Theatre and Arts facilitation, Corporate, Finance, Engineering and Event administration. Parks are included under this caption because of public entertainment that is provided in them.

Sanitation and Sewer

Sanitation and Sewer is responsible for the general cleanliness of the City including daily garbage collection and maintenance of the sewer system.

Public Works and Planning

Public Works and Planning provides maintenance services to ensure that roads, traffic lights, street lights, Corporation vehicles and equipment are in good working order. In addition, any future major construction development is handled by this segment.

Parking

Parking which includes both on and off-street parking is administered through this department. Consideration is given to the availability of car parking spaces in order to meet the public demand for parking.

Wharf

Wharf is responsible for the security of the waterfront in the City. Good working order of the docks for both cruise ships and cargo vessels is of prime importance for efficient transfer of goods and passengers through the port.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

12. **Segmented reporting** (continued)

	<u>2017</u>					<u>2016</u>	
	<u>Governance and Civic Services</u>	<u>Sanitation and Sewer</u>	<u>Public Works and Planning</u>	<u>Parking</u>	<u>Wharf</u>	<u>Total</u>	<u>Total</u>
Revenue							
Property taxes	\$ 2,886,204	\$ 2,886,204	\$ 2,886,205	\$ —	\$ —	\$ 8,658,613	\$ 8,588,847
Goods wharfage	—	—	—	—	6,894,793	6,894,793	6,322,083
Car parking fees	—	—	—	3,065,915	—	3,065,915	2,882,818
Sewer disposal contracts	—	2,286,314	—	—	—	2,286,314	2,284,546
Rents from properties	917,376	37,051	21,062	—	28,220	1,003,709	941,678
Other permit and license fees	150,231	187,731	—	—	232,823	570,785	435,120
Ships wharfage	—	—	—	—	420,601	420,601	358,940
Dock storage	—	—	—	—	286,920	286,920	188,424
City Hall rents	102,015	—	—	—	—	102,015	100,533
Miscellaneous	(8,174)	48,380	—	—	—	40,206	49,946
Interest	21,684	—	—	—	—	21,684	12,012
	<u>4,069,336</u>	<u>5,445,680</u>	<u>2,907,267</u>	<u>3,065,915</u>	<u>7,863,357</u>	<u>23,351,555</u>	<u>22,164,947</u>
Expenditures							
Wages, salaries and benefits	5,397,070	2,681,423	1,739,345	112,786	100,542	10,031,166	9,633,667
Contract services	3,381,382	1,106,861	1,585,505	67,082	1,161,675	7,302,505	7,566,382
Supplies and material	624,079	214,284	897,244	38,075	61,466	1,835,148	1,847,211
Amortization of tangible capital assets	249,420	295,809	436,158	343,563	361,432	1,686,382	1,646,563
Interest and finance	534,078	—	—	—	—	534,078	552,461
	<u>10,186,029</u>	<u>4,298,377</u>	<u>4,658,252</u>	<u>561,506</u>	<u>1,685,115</u>	<u>21,389,279</u>	<u>21,246,284</u>
Derecognition of liability on guarantee	<u>6,270,950</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>6,270,950</u>	<u>18,752,548</u>
Excess (shortfall) of revenue over expenditures	\$ <u>154,257</u>	\$ <u>1,147,303</u>	\$ <u>(1,750,985)</u>	\$ <u>2,504,409</u>	\$ <u>6,178,242</u>	\$ <u>8,233,226</u>	\$ <u>19,671,211</u>

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

13. Contingencies

- (a) In 2013, the law firm of J2 Chambers were paid a retainer of \$270,000 to represent the Corporation on various legal matters. In April 2015, the Corporation filed court proceeding against J2 Chambers to obtain copies of all invoices. Subsequently J2 Chambers filed a defamation suit against the Mayor and Secretary of the Corporation as a result of letters written to the Supreme Court and the Bar Council. The Chief Justice ruled that the law firm was to produce invoices to the Corporation, redacted if necessary. In addition to invoices the Corporation has requested confirmation of engagements and scope of work for matters not pertaining to the retainers paid. Invoices were received in July 2015. The Corporation is still pursuing legal action to obtain the legal files and have filed a complaint with the Bar Council and Attorney General. On July 27, 2016 proceedings were issued for possession of the Corporation's files and J2 Chambers was ordered to deliver the files to the Corporations' attorneys together with costs. J2 Chambers failed to forward the files and a judgement in default of appearance was obtained on February 23, 2017. Contempt proceedings against J2 Chambers were filed on April 26, 2017 when the files had still not been delivered. In June 2017 the Corporation was ordered to pay \$64,936 into courts which J2 claimed to be outstanding for professional services. Upon payment of the funds J2 was required to produce and forward all files, books and records including electronic data in its possession to the offices of the Corporation's attorneys. J2 failed to produce and forward the files so in January 2018, the Corporation filed an order for the funds to be released. J2 has also never made a claim for the funds paid into the courts. On February 15, 2018 the court ordered the funds be released to the Corporation's attorneys. The Corporation's request to be compensated for costs was denied. The funds are included in accounts receivable in the statement of financial position and were received on May 8, 2018.
- (b) On June 2, 2014, the Corporation commenced civil proceedings against the Attorney General to determine the Corporation's ability to regulate parking on its properties within the City. On November 5, 2014, Bermuda's Chief Justice ruled against the Corporation and determined the Hamilton Pay & Display Parking Vehicle Wheel Clamping Ordinance 2007 and the Hamilton Pay and Display Voucher Parking Amendment Ordinance 2010 were not valid since the Ordinances were not published in the Official Gazette and were not sent to the Cabinet Secretary for formatting, numbering and publishing. The Hamilton Traffic and Parking Ordinance 2013 which was published but not numbered by the Cabinet Secretary was also deemed to be invalid. These Ordinances were also retrospectively rendered invalid when section 17(2) of the Municipalities Amendment Act 2013 became effective in October 2013. In addition the Chief Justice ruled that the Corporation could not utilise its authority via a resolution but must use the authority of an ordinance. This ruling means that the Corporation currently has no legal authority to clamp or regulate vehicles illegally parked in the City. The Corporation lodged an appeal against the ruling in January 2015. The ruling has had a significant negative impact on the Corporation's parking revenue.
- On March 24, 2017 the Court of Appeals upheld the November 5, 2014 ruling that the Corporation could not utilise its authority via a resolution but must use the authority of an Ordinance. The Corporation must use the procedures in Section 38 of the Municipalities Act 1923 for the regulation and control of parking.
- (c) In 2016 MIF retained the services of a US law firm to initiate litigation against the Corporation and two of its officers and a third party claiming that their fraudulent, grossly negligent and conspiratorial actions resulted in the improper release of \$13,759,855 from an escrow account for the development of a luxury hotel and condominium residence at the Par-la-Ville car park. The parties named in the lawsuit were given 15 days from the date of the letter of October 15, 2016 to pay the funds to the US law firm. MIF is also seeking to recover consequential/special and punitive damages, as well as attorneys' fees, interest and costs. The Corporation's lawyers wrote to the US law firm and have asked for this matter to be set aside due to the Supreme Court appeal (Note 14). No further action was taken on this matter in 2016 and the US law firm confirmed that MIF would not be initiating proceedings pending resolution of the ongoing legal proceedings in Bermuda.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

13. Contingencies (continued)

- (c) In July 2017 MIF filed proceedings against the Bank of New York Mellon (BNY Mellon) and the Corporation in the Supreme Court of the State of New York. In December 2017 the attorneys for BNY Mellon advised that BNY Mellon would seek indemnification from MIF and the Corporation for any losses, including attorneys fees, incurred in the litigation. Under the terms of the escrow agreement, the right to indemnification, if it exists at all, cannot be determined until the litigation is over.
- (d) On August 1, 2017, the attorneys for the Corporation wrote to the receivers asking them to return any funds in their possession in relation to their appointment as receivers for the Par-la-Ville car park property. In response to the letter MIF filed a generally endorsed writ of summons in the Supreme Court of Bermuda on August 17, 2017. MIF's claim is for a declaration that the mortgage is valid and binding; a declaration that the appointment of the receivers is valid and binding; and a claim for further other relief and costs. They argue that the mortgage is an obligation discreet from the guarantee and enforceable in any event. Based on legal advice, the Corporation considers the mortgage document to be null and void since the Guarantee has been held to be ultra vires (Note 14).

14. Due to Mexico Infrastructure Finance LLC ("MIF")

In 2012, the Corporation entered into a Development Agreement and Ground Lease with Par-la-Ville Hotel and Residences Ltd ("PHRL") to build a luxury hotel and condominium residence in the Par-la-Ville car park (the "Project"). In November 2013 Section 20 of the Municipalities Act 1923 was amended and applied retroactively to any agreement for 21 years or longer entered into by the Corporation on or after January 1, 2012. Under Section 20, the agreement must be approved by the Legislature. The Par-la-Ville lease was approved by Parliament in November 2013.

Mexico Infrastructure Fund Limited ("MIF"), PHRL and the Corporation executed a credit agreement (the "Credit Agreement") on July 9, 2014 in which MIF agreed to loan PHRL \$18 million as bridge financing for the construction of the Project. The Credit Agreement was executed on the basis that the Corporation agreed to:

1. provide a mortgage over the property known as the Par-la-Ville car park (the "Property"); and
2. guarantee the loan (the "Guarantee").

In March 2013, the Minister gave permission for the Corporation to grant MIF a mortgage over the Property. On March 28, 2013 the Corporation passed a resolution to pledge the car park property as collateral. On December 16, 2013 the Corporation passed a resolution to provide the Guarantee for the loan. In June 2014, Section 37 of the Municipalities Act 1923 was amended, purportedly to enable the Corporation to provide the Guarantee. On July 9, 2014 the Minister gave permission for the Corporation to provide the Guarantee.

On July 9, 2014, an escrow agreement was entered into between MIF, PHRL, the Corporation and BNY Mellon ("the Escrow Agent"). Under the terms and conditions of the escrow agreement, the Escrow Agent was to hold the loan proceeds until such time as PHRL had secured permanent financing comprising debt of \$225 million and equity of \$100 million or a "substantially similar financing structure from the Permanent Lender". The Corporation authorized the release of the funds from the escrow account in October 2014 based on an agreement reached between PHRL and Argyle Limited, a company which PHRL represented to the Corporation as the "Permanent Lender".

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

14. **Due to Mexico Infrastructure Finance LLC (“MIF”)** (continued)

Due to the default on repayment of the loan by PHRL, on December 30, 2014 MIF initiated legal proceedings against the Corporation and PHRL. On March 31, 2015, Joint Receivers were appointed over the Property. On May 27, 2015, the Supreme Court awarded summary judgment to MIF over claims against PHRL and the Corporation. The judgment against the Corporation was for \$18 million and accrued interest from the date of judgment at the rate of 7% per annum or \$3,452 per day until the obligation is satisfied. As a result of the judgment, MIF was not limited to proceeding against the Par-La-Ville car park to obtain satisfaction of its judgment against the Corporation, as the judgment provided for the extension of MIF’s equitable rights to all of the Corporation’s assets. In September 2015 MIF filed a summons to garnish the bank accounts and a writ to seize the assets of the Corporation with the Supreme Court of Bermuda in an effort to receive payment to satisfy the judgement. To date no action has been taken pending the result of further ongoing legal proceedings.

In accordance with the terms of the Credit Agreement, PHRL was due to pay the Corporation \$900,000 upon the closing of financing from the Permanent Lender. In July 2015, the Corporation issued a statutory demand for payment. PHRL did not make this payment and on August 28, 2015 the Corporation petitioned the Supreme Court to wind up PHRL in accordance with Section 161 (e) of the Companies Act 1981. Joint provisional liquidators were appointed over PHRL on October 9, 2015.

In December 2015, the House of Assembly passed an amendment to the Municipalities Act, permitting the Corporation to increase their debt limit from \$20 to \$30 million, thereby allowing a loan to be obtained to cover the \$18 million plus interest due to MIF. The Corporation negotiated with a local bank to acquire a bank loan. The terms and conditions of the loan were approved by Parliament in March 2016 in accordance with Section 20 (1) of the Municipalities Act. The bank loan has been put on hold pending the outcome of the ongoing legal proceedings.

On June 14, 2016, the Corporation submitted an application to the courts to overturn the summary judgement made in May 2015 by the Chief Justice on the basis that the guarantee issued to MIF was outside the remit of the Corporation.

On November 18, 2016, the Supreme Court ruled that the Corporation had no power to guarantee the loan from MIF to build a hotel on the Par-la-Ville car park. The Court resolved that in providing the guarantee, the Corporation had acted ultra vires. Therefore, the previously unchallenged Consent Order that had required the Corporation to pay MIF the loan plus interest was set aside. The Corporation ceased accruing interest on the due to MIF balance of \$18 million with effect from November 18, 2016. The judge’s decision was appealed by MIF in the March 2017 session of the appellate court. In the March 2017 session, the Corporation also appealed the judge’s decision not to award costs to the Corporation. On May 12, 2017 the Court of Appeal dismissed the appeal and upheld the Supreme Court ruling that (i) in providing the guarantee, the Corporation acted ultra vires and (ii) the Corporation’s application to set aside the Consent Order was not an abuse of process. Therefore the guarantee cannot be enforced against the Corporation and the Corporation is not liable for the guaranteed sum of \$18 million. In June 2017 MIF served notice of its application to appeal this decision to the Privy Council.

As the guarantee cannot presently be enforced against the Corporation and the Corporation is not liable for the guaranteed sum of \$18 million the Corporation has derecognised the liability related to the guarantee of \$18 million together with previously accrued interest of \$752,548 and this reversal of \$18,752,548 is included in the statement of operations for the year ended December 31, 2016. The Privy Council hearing will be held in October 2018 with a decision expected shortly thereafter.

CORPORATION OF HAMILTON

Notes to the Financial Statements

December 31, 2017

(Expressed in Bermuda Dollars)

14. **Due to Mexico Infrastructure Finance LLC (“MIF”)** (continued)

The Joint Provisional Liquidators of PHRL have brought proceedings in the High Court of Justice in England against a number of parties in order to recover funds loaned to PHRL and subsequently transferred to Argyle Limited. As the creditor who appeared to have the major economic interest in the liquidation of PHRL at the time, the Corporation agreed, in August 2016, to place a deposit of \$275,000 with the courts for these proceedings to cover any potential costs should the Corporation lose the case. The Corporation expects a successful outcome to this case and that the full deposit will be returned. However as the recovery of the deposit is contingent on the outcome of the ongoing proceedings the deposit of \$275,000 has been expensed and was included in administrative and general expenses in the statement of operations for the year ended December 31, 2016.

In May 2016, the Corporation provided funding of \$25,000 for the winding up of Argyle Limited and in August 2016 a further \$100,000 was provided to fund the liquidation of PHRL, the Skyline Trust and Argyle Limited. In the event of recoveries by the Joint Provisional Liquidators these funds will be returned to the Corporation.

15. **Subsequent events**

The Corporation evaluated events and transactions occurring from January 1, 2018 through to May 9, 2018, for potential recognition or disclosure in the notes to the financial statements.

Management believes that there are no other post year-end events that need to be reflected in the financial statements or disclosed in the notes to the financial statements.

On March 9, 2018 the Minister of Home Affairs (the “Minister”) announced changes to the Act via the Municipalities Amendment Act 2018. The amendments will provide for the Minister to authorize public officers to attend meetings of the Corporation, for the Minister to give directions and take stewardship or temporary control of the Corporation in certain circumstances where he believes it is in the best interests of Bermuda, and for the next ordinary municipal election to be held in 2019, not 2018. The Act was passed by the Bermuda Parliament in March 2018. As per the Ministerial statement, during the next year the Government will undertake consultations with the relevant stakeholders to determine the most appropriate method to strengthen and modernize municipal governance for the benefit of Bermuda.

On March 28, 2018 the Corporation of Hamilton signed a Memorandum of Understanding (“MOU”) with the aim to purchase a local franchise in the near future at a potential price of \$795,000.

On May 5, 2018 a senior officer and the former Mayor of the Corporation were summoned to appear in the Bermuda Magistrates Court on June 4, 2018 with respect to the amount due to MIF (see Note 14). The Corporation has not been named in the summons. On June 1, 2018, the Corporation agreed to cover the initial legal fees in the amount of \$15,000 for each individual respectively, until Directors and Officers (“D&O”) insurance coverage can be confirmed.