

Date: October 16, 2020	Originator's files:
To: Chair and Members of Budget Committee	
From: Gary Kent, CPA, CGA, ICD.D, Commissioner of Corporate Services and Chief Financial Officer	Meeting date: November 23, 2020

## Subject

**Municipal Act Reporting Requirements Under Regulation 284-09**

## Recommendation

That the report dated October 16, 2020, entitled "Municipal Act Reporting Requirements Under Ontario Regulation 284/09" from the Commissioner of Corporate Services and Chief Financial Officer be approved.

## Report Highlights

- In accordance with Ontario Regulation 284/09, an annual report must be presented to Council which outlines the estimated expenses that will be included in the annual financial statements but are excluded from the 2021 budget, and the impact of these differences on the accumulated surplus. The report should also include an analysis of the estimated impact on the future tangible capital asset funding requirements.
- Amortization and post-employment benefits expenses are included in the City's financial statements. If amortization and post-employment benefits were not included in the City's financial statements, the accumulated surplus at the end of the year would be \$147.1 million higher.
- Regulation 284/09 does not require other adjustments to be disclosed in this report. If all differences between the annual financial statements and the 2021 budget were disclosed, the annual financial statements would show a deficit of \$0.1 million.
- The City provides for the replenishment of its assets through contributions to its reserve funds, debt and from funding from other levels of government. The 2021 budget proposes that \$118 million be spent in the tax funded budget and \$31.8 million in the storm water charge funded budget for infrastructure renewal.

- The 2021 budget proposes that \$2.1 million be provided to fund current post-employment benefit payments. The City has a balance of \$35.6 million in its Employee Benefits Reserve Fund which may be used to offset the estimated liability of \$68.1 million.

## Background

The Municipal Act requires that municipalities prepare annual financial statements that are in accordance with generally accepted accounting principles (GAAP) for local governments as recommended by the Public Sector Accounting Board (PSAB) of the Chartered Professional Accountants of Canada (CPA Canada). PSAB standard 3150 requires the recording of the cost of tangible capital assets and related annual amortization expense on municipal financial statements.

The budget is prepared on the cash basis of accounting which differs from PSAB in that revenue and expenses are recorded when received or spent rather than accrued in the year in which they are earned or measurable. The budget accounts for liabilities in whole or in part by setting aside funds for future use in reserves. There is no amortization or depreciation of assets, or deferral of development charges or other fees. These are recorded when received. Reserves may be increased or decreased through transfers between funds and not accounted for as a revenue or expense.

The budget is prepared in accordance with the requirements of the Municipal Act, notwithstanding that it is prepared on a different basis of accounting from the annual financial statements. Ontario Regulation 284/09 was introduced as an attempt to reconcile the major differences between the annual financial statements and the budget. This regulation requires formal reporting to advise Council of the impact of not including these items. This report is required to be prepared and adopted at the time the budget is approved.

Regulation 284/09 requires a Corporate Report to be prepared for Council's adoption by resolution that identifies the impacts of not including amortization expenses, post-employment retirement benefits and solid waste landfill closure and post-closure expenses in the budget. Specifically, the report must provide an estimate of the change in the accumulated surplus of the municipality resulting from the exclusion of any of these expenses, and an analysis of the estimated impact of the exclusion of any of the expenses on the future tangible capital asset funding requirements of the municipality.

## Comments

The purpose of the PSAB requirements in the annual financial statements is to fairly present the financial position of the City at a point in time (i.e., year end, which is December 31 for municipalities in Ontario). The financial statements require estimates of various liabilities, prepaid expenses and deferred revenues, and other items. These are disclosed in the Significant Accounting Policies Note 1 to the annual financial statements.

The budget is not an accounting of the City's financial position at a point in time. It is a spending control document, a revenue rate setting document and the means to calculate a property tax levy. This is specified in section 290 on the Municipal Act, "A local municipality shall, in the year or the immediately preceding year, prepare and adopt a budget including estimates of all sums required during the year for the purposes of the municipality..." Section 312 of the Municipal Act goes on to state "general local municipality levy means the amount the local municipality decided to raise in its budget for the year under section 290 on all rateable property in the local municipality..."

From time to time, municipalities have come under criticism from groups like C.D. Howe Institute that the budget should be prepared on the same basis of accounting as the annual financial statements to ensure that Council and the public are aware of the impact of not fully providing for all liabilities incurred by the City, and that by not doing so, the City is indebting future generations with costs incurred today.

It is the view of Finance staff, that the City does provide this information through adoption of PSAB in the annual financial statements, the provision of the approved budget in the annual financial statements, which allows comparison of actual financial results to the budget estimates, and the provision of note 16 to the annual financial statements, which adjusts the approved budget to the same basis of accounting as the annual financial statements to allow for more meaningful comparison of actual and estimated budget results.

Further, the City provides through this report, both the information required to comply with regulation 284/09 and a reconciliation between the budget as proposed to Council and the budget as if it were presented on a PSAB basis. This reconciliation is shown in the financial impact section of this report and has been reproduced in its entirety from that shown in the 2021 budget book on page T-10. (There will be a difference between the surplus/deficit shown in the budget book and that contained in note 15 to the annual financial statements because the former is an estimate based upon information known earlier in the year compared to the annual financial statements for which actual information at year end is available).

It is important to note that there is a difference between a requirement to account for a revenue, expense or liability on a PSAB basis and actually receiving, spending or providing for those amounts with actual cash. The concern with fully funding in the budget all liabilities as identified through PSAB accounting is first that liabilities are an estimate at a point in time which can change in subsequent accounting periods and second that not all liabilities will need to be funded, or can be funded in another manner. For example, vacation pay does not need to be funded because it is the practice of the City to require employees to take their annual vacation, and in the year of retirement or leaving, the City does not incur replacement employee salaries because positions are not filled until the actual retirement date of the employee, which includes unused vacation time. Thus there is no additional cost to the City beyond the normal salary which would be paid to the employee regardless. Similarly, although the budget does not provide for amortization it does set aside funds through its reserves to pay for future renewal of its infrastructure. The budget also contains funding contributions from other levels of government (e.g., Gas tax and infrastructure funding, applied to infrastructure renewal) and debt funding.

## Financial Impact

The following table is a reconciliation between the budget as proposed to Council and the budget if it were presented on a PSAB basis. This table is reproduced in its entirety from page T-10 of the budget book. Overall, there would be deficit of \$0.1 million which combines the property tax base and the stormwater program. On a PSAB basis, the tax levy would need to be increased by \$27.0 million or 1.8% on the total residential tax bill.

Description	Property Tax Base (\$M)	Stormwater (\$M)	Consolidated (\$M)
<b>Proposed 2021 Net Operating Budget</b>	<b>554.4</b>	<b>0.0</b>	<b>554.4</b>
<b>REVENUE</b>			
<b>Proposed 2021 Operating Revenue</b>	<b>412.0</b>	<b>43.5</b>	<b>455.5</b>
<b>Add:</b>			
Property Tax Revenue	554.4		<b>554.4</b>
Reserve funds interest	18.2	3.8	<b>22.0</b>
Recoveries	13.1		<b>13.1</b>
<b>Less:</b>			
Contributions from reserves and reserve funds	(86.4)		<b>(86.4)</b>
Enersource dividend	(16.6)		<b>(16.6)</b>
City budgeted levy for Business Improvement Associations (BIA)	(1.5)		<b>(1.5)</b>
<b>Full Accrual Revenue Budget</b>	<b>893.2</b>	<b>47.3</b>	<b>940.6</b>
<b>EXPENSES</b>			
<b>Proposed 2021 Operating Expenses</b>	<b>966.4</b>	<b>43.5</b>	<b>1,010.0</b>
<b>Add:</b>			
Amortization (Depreciation Expense)	136.5	8.5	<b>145.1</b>
<b>Less:</b>			
Contributions to reserve and reserve funds	(146.7)	(30.8)	<b>(177.5)</b>
Debt principal repayments	(34.5)	(0.9)	<b>(35.4)</b>
BIA budget on City's books	(1.5)		<b>(1.5)</b>
<b>Full Accrual Expense Budget</b>	<b>920.3</b>	<b>20.4</b>	<b>940.7</b>
<b>Net Surplus/ (Deficit)</b>	<b>(27.0)</b>	<b>26.9</b>	<b>(0.1)</b>

O.Reg 284/09 requires the City to provide an estimate of the change in the accumulated surplus of the municipality resulting from the exclusion of amortization expenses, post-employment benefits expenses and solid waste landfill closure and post-closure expenses, and an analysis of the estimated impact of the exclusion of any of these expenses on the future tangible capital asset funding requirements.

If these expenses were not included in the City's financial statements, the accumulated surplus at the end of the year would be \$147.1 million higher.

The estimated amortization expense based upon the historical cost of the underlying assets, in accordance with PSAB requirements is \$145.1 million. Page B-79 of the budget book proposes \$118 million be spent on infrastructure renewal in the tax funded budget, for a funding gap of \$291 million when compared to replacement value. The storm water budget proposes \$31.8 million be spent on infrastructure renewal.

## Conclusion

The City is required by O.Reg 284/09 of the Municipal Act to prepare and have Council approve an annual report prior to adopting the budget which identifies the changes in accumulated surplus if amortization and post-employment benefit expenses were excluded from the full accrual budget. If these expenses were not included in the City's financial statements, the City's 2021 accumulated surplus would be \$147.1 million higher.

O.Reg 284/09 only requires that the impact of amortization and post-employment benefit expenses be disclosed. There are other differences in the basis of accounting used in the 2021 budget and the annual financial statements. If these other differences are accounted for, the annual financial statements would show a deficit of \$0.1 million.

The City provides for the replenishment of its assets through contributions to its reserve funds and from funding from other levels of government as well as the issuance of debt. The 2021 budget proposes that \$118 million be spent in the tax funded budget and \$31.8 million in the storm water funded budget for infrastructure renewal.

The 2021 budget proposes that \$2.1 million be provided to fund current post-employment benefit payments. The City has a balance of \$35.6 million in its Employee Benefits Reserve Fund which may be used to offset the estimated liability of \$68.1 million.



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