Subject: 2025 Operating Budget Reconciliation and Financial Disclosure O. Reg 284/09

Report to: Budget Review Committee of the Whole

Report date: Thursday, December 5, 2024

Recommendations

1. That this report **BE RECEIVED** for information.

Key Facts

- The purpose of this report is to reconcile the Region's budget, which is prepared in consideration of its cash needs for the year against the Public Sector Accounting Standards (PSAS) presentation, which would include non-cash items.
- Municipal budgets are prepared primarily on a cash basis for setting the general and special tax levies and water and wastewater rate requisitions. This includes the items such as principal debt repayments and transfers to reserves.
- Ontario Regulation 284/09 Budget Matters – Expenses (O.Reg 284/09), requires that before adopting a budget for the year that excludes non-cash items, a municipality must prepare a report to council about the excluded expenses.
- This report identifies the components that reconcile the Region's balanced operating budget to the estimated financial statement operating surplus of $269.7 million to be reported in the Region's annual financial report in accordance with Public Sector Accounting Standards.

Financial Considerations

When preparing the budget, the Region considers its cash needs for the year to ensure it collects sufficient tax revenue to cover its obligations and execute its business plan. This includes budgeting for principal debt repayments and considers required transfers to reserves. Conversely, the Region does not budget for amortization of capital assets, accretion for asset retirement obligations, changes in employee future benefits liabilities, and changes contaminated site liability, as these are primarily non-cash items.

A requirement of the regulations is for Niagara Region to reconcile the approved budget to PSAS. Had we budgeted for non-cash items and excluded cash requirements for debt principal payments and reserve transfers we would have a total PSAS operating surplus of $269.7 million as per Table 1.

Table 1 – 2025 PSAS Adjusted Budget (in millions)

Description	2025 Budget
Budgeted Operating Surplus	$ 0
Non-Cash items	
Amortization	(107.7)
Accretion	(2.7)
Employee Future Benefits Increase	(5.8)
Total Non-Cash Items	(116.2)
Cash Items	
Capital Project Expenditures not resulting in Tangible Capital Assets	(10.1)
Operating Expenditures resulting in Tangible Capital Assets	2.2
Principal Debt Repayments	48.3
Total Net Transfers to Reserves	145.0
Total Cash Items	185.4
PSAS Operating Surplus	69.2
Capital Fund revenues	200.5
Total PSAS Operating Surplus	269.7

If the Region were to adopt budgeting on a PSAS accrual basis, the budget would need to include the non-cash expenditures of amortization, accretion for asset retirement obligations, and employee future benefits as well as the cash items resulting in a PSAS Operating Surplus of $69.2 million before capital fund revenues. This means the Region requires $69.2 million more to pay for operations than would be available with the PSAS accrual based budget.

Capital Fund revenue and expenditures would not have a budget impact under PSAS as these revenues are project specific and from external parties. Some examples of these revenues are development charges, Canada Community Building Fund, 3rd party grants and cost recoveries.

Analysis

This section provides further analysis into assumptions of the adjusted items.

Tangible Capital Assets

Amortization is a non-cash expense reflecting the estimated usage of our tangible capital assets in the financial statements over time. For purposes of this report the 2025 budget for amortization has been estimated at $107.7 million (Table 1). The differential between the estimated amortization and proposed capital funding from reserves in the 2025 Capital Budget is approximately $67.9 million. Amortization reflects the historical cost of the asset and does not take into consideration current replacement costs. Budgeting for amortization alone does not support the Region’s future capital needs, nor does it properly consider the Region’s asset funding strategies. Budgeting for amortization alone would result in a cash flow deficit to the Region.

Asset Retirement Obligations

On January 1, 2023, the Region adopted PS 3280 Asset Retirement Obligations on a prospective basis. The adoption of the accounting policy has impacted the Region’s statement of operations by recognizing $3.7 million of accretion expense in 2023 which is comprised of obligations related to asbestos, landfill closure and post-closure and leases. Accretion is a non-cash expense that is recognized with the passage of time and increases the present value of the liability for the asset retirement obligation. The forecasted accretion for 2025 is $2.7 million which includes $2.4 million accretion related to the Landfill Liability.

If solid waste landfill closure and post closure liability costs were included in the budget the accumulated surplus would decrease by $2.4 million as we are anticipating that the liability will increase from $141.8 million to $144.2 million during 2025. The forecasted balance of the Region’s Landfill Liability reserve at December 31, 2024 based on the Q3 financial update is $4.0 million.

Based on closure and post closure cost projections as of December 31, 2024 the estimated operating and capital costs for 2025 are $2.4 million. The Region has two remaining open landfill sites for which the closure and post-closure costs have been reflected in the liability.

Employee Future Benefits

In 2025, it is estimated that the Region's Employee Future Benefits (EFB) liability will increase by $5.8 million from $142.2 million to $148.1 million. If the forecasted growth in the EFB liabilities was budgeted, in addition to the projected cash payments, the impact would be a reduction in the accumulated surplus by approximately $5.8 million (the increase in estimated liability during 2025). The forecasted balance of the Region's EFB reserves at December 31, 2024 based on the Q3 financial update is $33.2 million. Any unfunded growth in the EFB liability could impact the Region's credit rating in the future.

Contaminated Sites

Similar to the EFB and accretion for asset retirement obligations, the Region does not budget for liabilities related to contaminated sites. As of December 31, 2023, there is a liability recorded of $0.58 million for contaminated sites. The liability will be re-evaluated at December 31, 2024. This reflects the estimated costs to remediate the contamination in 2028 subject to Council approval. At this time, the liability is not anticipated to change and therefore would not impact the accumulated surplus.

Prior Year Reconciliation of the Disclosure Report and Financial Statements

This report contains forward-looking information; a number of factors could cause actual results to differ from the financial estimates disclosed in this report. The following table compares the 2023 budget disclosure requirement against the most recent audited financial statements (2023).

Table 2 – 2023 Regulatory Disclosure vs 2023 Audited Financial Statement (in millions)

Description	Disclosure Report	Financial Statement
Operating Surplus	$ 0	$7.1
Non-Cash items		
Amortization	(99.6)	(107.7)
Accretion		(3.7)
Gain (Loss) on Transfer of Capital Assets		65.9
Employee Future Benefits Increase	(6.6)	(9.1)
Landfill Liability Increase	4.0	0.4
Total Non-Cash Items	(102.2)	(54.2)
Cash Items		
Capital Project Expenditures not resulting in Tangible Capital Assets	(9.9)	(7.1)
Operating Expenditures resulting in Tangible Capital Assets	2.7	2.3
Principal Debt Repayments	54.0	34.9
Total Net Transfers to Reserves	75.6	114.1
Total Cash Items	122.4	144.2
PSAS Operating Surplus	20.2	97.1
Capital Fund revenues	84.8	86.7
Total PSAS Operating Surplus	105.0	183.8

At the time the 2023 Budget was approved, and this report prepared, staff had estimated and reported to Council a financial statement surplus that was actually lower than the actual PSAS surplus by $76.9 million ($97.1 million less $20.2 million). An explanation of the primary variances are as follows:

- Gain on Transfer of Capital Assets was primarily a result of establishing the Niagara Transit Commission (the "Commission"), effective January 1, 2023. Upon establishing the Commission, the Region assumed tangible capital assets from the City of Niagara Falls, City of St. Catharines, City of Welland and Town of Fort Erie in the amount of $79.1 million.
- Adoption of PS 3280 on January 1, 2023 resulted in the Region recognizing $3.7 million of accretion expense.

- Changes in modeling of estimates to the Employee the Future Benefit and Landfill Liability.
- Capital Project expenditures not resulting in Tangible Capital Assets are caused primarily by capital items below the capitalization threshold, Regional grants to transit providers for buses, consulting, engineering and professional services that may have been incurred that did not lead to completion of a capital asset.
- Principal debt repayment are lower as the Region only debentures when a capital project has been substantially complete.
- COVID funding requirements decreased by $17.7 million, resulting in an increased Net Transfers to Reserves.
- Capital revenues are budgeted in full in the year the capital budget is approved and does not always correspond to the date it is earned and recorded in the audited financial statements.

Alternatives Reviewed

No alternatives were reviewed as all municipalities are required to comply with Ontario Regulation 284/09.

Relationship to Council Strategic Priorities

This report was written to comply with Ontario Regulation 284/09. There are no direct links between this report and Council Strategic Priorities.

Other Pertinent Reports

CSD 64-2024 Consolidated Levy 2025 Operating Budget

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