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UPDATE RE CAPITAL ASSET MANAGEMENT PROJECT

The Finance and Administration Committee recommends the adoption of the recommendation contained in the following report from the Commissioner of Finance:

1. RECOMMENDATION

It is recommended that this report be received for information.

2. PURPOSE

The purpose of this report is to provide an update on the Region's preparations for expected recommendation from the Canadian Institute of Chartered Accountants (CICA), Public Sector Accounting Board (PSAB) requiring local governments to report capital assets in their financial statements by 2006 and capital asset accounting by 2008. This information is also being compiled to determine the adequacy of the Region's reserve funds for asset replacement, and a long term strategy to provide funding to tax reserves.

3. BACKGROUND

The CICA's PSAB is responsible for setting the accounting and financial reporting standards for all levels of government in Canada. In 2003, a research report titled Accounting for Infrastructure in the Public Sector was released. The study group that produced this report conducted extensive reviews of international and Canadian practices of accounting for capital assets in both the private and public sector.

The study group concluded that there are various benefits to providing information about capital assets but, at the local level, there is a significant gap between the financial information management and municipalities need to manage their capital assets and the information they currently receive.

If the cost of using infrastructure is not reported, that cost cannot be taken into account and governments cannot adequately exercise their stewardship responsibilities. Further, without understanding the future maintenance and replacement costs associated with infrastructure, governments cannot easily assess whether they can afford to maintain existing programs or expand both the type and quality of those programs.

The study also looked at how financial statements, and the information they are based on, could fill the financial information gap referenced above. While a variety of factors were recognized during the study which led to a number of conclusions, it was generally concluded that this information would contribute significantly towards filling the gap identified.

It is expected that the PSAB Task Force on the Financial Reporting Model for Local Government will consider the conclusions of the study as part of the current review. Recording capital assets in the financial statements is the last hurdle to bring local government financial statements to full accrual accounting basis. Since Canada's senior levels of government now report capital assets in their financial statements, it is expected that PSAB will recommend the extension of this reporting to local governments by 2006 and will require capital asset accounting by 2008.

Responses to the study's conclusions have been submitted by the Municipal Finance Officers Association (MFOA) and the Association of Municipal Managers, Clerks and Treasurers of Ontario (AMCTO) and by York Region to the CICA's PSAB, specifically on Tangible Capital Assets.

4. ANALYSIS AND OPTIONS

4.1 Project Research

An internal project to identify and value all significant capital assets and infrastructure was initiated in early 2005 by the CAO and Commissioner of Finance in order to develop a long-term comprehensive capital asset replacement funding strategy model. The first phase, data collection and valuation, is expected to be completed by December 31, 2005.

A guiding principles team was established to develop capital asset descriptions and structures; estimate useful lives and determine capitalization thresholds for this project.

To date, most significant discrete and linear assets have been identified using formal or informal departmental inventories, property records, consultant's reports and studies, and insurance records. Assets identified include kilometres of water and wastewater piping by diameter, kilometres of roads by road section, all bridges and culverts, all owned buildings, buses, ambulances and other vehicles, wells, elevated towers, in-ground reservoirs, etc.

Asset replacement cost values are being estimated using several methods. The current replacement cost insurance appraisal of discrete assets being conducted for the Region's insurance branch will provide baseline cost data for a large segment of the inventory. The asset inventory has been helpful to ensure that the Region's insurance program includes all assets exposed to risk. Asset valuations performed by other external consultants, such as done for the water and wastewater rate study, are used to value portions of the inventory. For other assets, engineering estimates or current average purchase or contract prices will be used.

An estimated life cycle of each asset category has been determined through discussion with staff and consultants, industry norms, or research of similar infrastructure asset life cycles used in North America, such as, for example, by the Province of Ontario.

By the end of December, 2005 a first pass of the inventory, valued at current replacement cost, together with the timing of replacements over the next fifty [50] years will be available. In addition to using this data to develop funding strategies, the data will also be used in the OMBI pilot project to help evaluate the impact of the change in accounting on financial statements and reserves.

As illustrated above, a significant amount of research and follow-up work has been completed to date and will contribute to the success of this project. In addition, it should position York Region well in terms of its participation in the OMBI pilot project on this topic, specifically related to the Roads Assets.

Regional Council at its meeting of June 23, 2005:

> *"endorsed the development of a proposal to be submitted for consideration of York Region as a pilot site for Accounting for Capital Assets project sponsored by the Ontario Municipal Benchmarking Initiative (OMBI)."*

With Council's approval granted, the guiding principles team developed the Region's proposal to OMBI to participate in the Pilot Project. In lieu of proposing that the Region include all assets in the Project, the team recommended undertaking a Pilot Project for the Roads branch only in order to do a more in-depth analysis of a significant infrastructure element.

The process of developing the capital asset structures and definitions and the final result will be used for the 2005 project and also as a starting point for the pilot project and the now expected 2008 or 2009 implementation by the CICA's PSAB.

The next phase of the Region's overall capital asset management plan will be:

- Determine appropriate reserve fund levels to address replacement/rehabilitation of major capital assets.

- Develop long term strategy to meet reserve fund adequacy levels.

4.2 Water & Wastewater Capital Assets

The operating costs associated with the provision of water and wastewater services are recovered through a uniform region-wide water and wastewater user rate, based on actual flows per cubic metre. A fixed component of each user rate is contributed to a reserve which is used to fund the replacement and rehabilitation of water and wastewater infrastructure. These reserves are also used to mitigate any large fluctuations in the water and wastewater user rates.

As part of the capital asset management project, identifying the elements representing a full costing methodology has been carried out through this review, with the consultant just concluding their work on this engagement.

The scope of activities carried out in this engagement included:

- Projection of operating cost requirements
- Analysis of annual replacement and major rehabilitation requirements
- Review of the Region's growth-related capital plan and the impact of continued residential development change discounting on user rate and reserve requirements
- Analysis of long-term user rate and capital replacement reserve implications resulting from operating and capital cost pressures
- Review of other jurisdictions regarding methods used to fund long-term capital infrastructure requirements, the use of reserve funds and reserve fund provisions

Completion of the *Water and Wastewater Servicing User Rate & Reserve Fund Adequacy Review* concludes a significant step in the capital asset management project, as it addresses the operating, capital rehabilitation, capital replacement and reserve requirements for a group of assets representing one of the largest components of the Regions capital asset inventory.

The financial impact of this review will begin to be reflected in the 2006 business plan and budget. The conclusions and recommendations from this review, upon completion of administrative review, will be the subject of a future presentation.

5. FINANCIAL IMPLICATIONS

The research associated with this project and participation in the OMBI pilot project are underway, commencing in 2005 and continuing throughout 2006. The 2005 and 2006 proposed operating budgets accommodate these projects.

The financial implications related to the maintenance of a capital asset accounting system, and the long term strategy to reach the required reserve fund levels will be the subject of future reports.

6. LOCAL MUNICIPAL IMPACT

There are no local municipal impacts to report.

7. CONCLUSION

Progress is continuing in the development of a long-term comprehensive capital asset replacement funding strategy model. In addition, an OMBI pilot project Site Manager, responsible for managing the project participants, process and deliverables, has been selected. The site manager will report to the OMBI Project Manager and also to the York Region Steering Committee for the duration of the project.

The Senior Management Group has reviewed this report.