Meeting Date: **November 15, 2023**

Submitted by: **Tiffany Farrell, Director of Corporate Services**

Report No: **CPS-54-2023**

Subject: **Asset Retirement Obligation Policy**

Recommendation:

That Report, CPS-54-2023, Asset Retirement Obligation (ARO) Policy be received;

AND THAT Policy appended to Report CPS-54-2023 be approved.

Purpose:

The purpose of this report is to provide information on the new Accounting Standard Section PS3280 of the Public Sector Accounting Board (PSAB) which has come into effect for years beginning on or after April 1, 2022 and to approve the associated policy.

Background:

Section PS3280 is a new requirement set out from PSAB (Public Sector Accounting Board) and all local governments will need to incorporate this standard into their financial statements for their 2023-year ends. Staff have been working on this requirement over the past year.

An asset retirement obligation (ARO) arises when there is a legal obligation to retire tangible capital assets. Retirement is defined as removal of a capital asset from service and includes sale transactions, asset abandonment and/or asset disposal. These costs may include (but are not limited to) dismantling and remediation of a tangible capital asset. Existing laws, regulations, and contractual agreements within the Municipality may require us to take specific actions to retire certain tangible capital assets at the end of their useful lives. The exercise of identifying, assessing, and estimating asset retirement obligations did require a considerable effort across the Municipal organization and involved outside specialists to complete.

Analysis:

This PSAB standard will require recognition of future costs related to the retirement of specific Municipal tangible capital assets. Investigation and evaluation work involved all departments and began early 2023. The valuation and recognition for the Municipality's AROs will be presented in the financial statements for the year ended December 31, 2023, with comparatives for 2022. Implementation of this new standard is a requirement of the Public Sector Accounting Board, and it is not optional.

The addition of AROs is a change in accounting policy. Changes in accounting policies need to be applied retrospectively, which means that the accounting records be adjusted as though the new accounting policy had always been in place, so that the opening equity balance of all periods presented incorporates the effects of the change.

Currently, the Municipality's financial statements reflect balances and disclosures aligned with public sector accounting standards addressing general liabilities, landfill liabilities, contractual obligations, contaminated sites, and contingent liabilities. The new measure extends these requirements to include liabilities related to the retirement of existing assets. The standard outlines that recognizing the cost of an asset should consist of the expenses incurred to retire that asset in the future. An ARO exists when there is a legal obligation to incur retirement costs concerning an asset. Some examples of when a legal obligation may exist:

- Lease requires removal of leasehold improvements at the end of the lease;
- Land covenants needing removed from a site at the end of their useful life;
- Assets that need to be returned to its natural state when assets are no longer in use;
- Assets that require compliance with standards and regulations that, if sold, disposed of or no longer in use, would require remediation, such as asbestos in buildings and in-ground piping.

The assets that have an associated retirement obligation for Middlesex Centre included buildings, underground storage tanks, wells and gravel pits.

Once an ARO liability is estimated, liability and asset of equal value are recorded on the Statement of Financial Position. This effectively increases the carrying cost of the existing asset at the same time as registering the liability. If the asset is no longer in use, then the liability for the ARO will be expensed immediately rather than creating an asset. Estimates will include all costs directly related to the asset retirement activities but will be limited to those legally enforceable. An estimate is made today for some point in the future, at which time the liability will be extinguished. The future value is then discounted through a discount rate. Each year there will be an accrued expense in the Statement of Operations to increase the liability with time. This recognizes the expense while the asset is in use and results in the liability growing to equal the estimated costs on the date of retirement of the asset. Like amortization, this is a non-cash expense item and does not directly drive budgeted revenues. However, there is a cost to be incurred in the asset's ending life, for example, with removing asbestos, which will need to be considered, how it will be funded when the cost-effectively occurs. Staff have created a new Asset Retirement Obligations Policy to establish the steps to be followed regarding recognition, subsequent measurement, and staff responsibilities.

It is important to note that the costs to remediate are just estimates.

Financial Implications:

Impacts will be reflected in the 2023 financial statements for the obligation costs in 2023 and 2022.

Costs to complete the building reviews for designated substances was $27,877.16.

Strategic Plan:

This matter aligns with following strategic priorities:

- Responsive Municipal Government

This report and policy is a legislative requirement under Public Sector Accounting Standards and additionally it responds directly to Objective 5.3 – Foster a culture of innovation, continuous improvement, and cost-effective services by sharing information and gathering input, by continuing our timely and effective communication to the public.

Attachments:

A1 Asset Retirement Obligation Policy