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## MANAGEMENT REPORT

**Date:** January 17, 2023  
**To:** Finance and Labour Relations Sub-committee  
**From:** Karmen Krueger, CPA, CA, Director of Corporate Services  
**Report #:** FIN23-005  
**Attachments:** 1. Draft Asset Retirement Obligation Policy  
2. Draft Workplan Implementation PS 3280 - ARO

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**Title:** Asset Retirement Obligations (ARO)

**Objective:** The purpose of the Asset Retirement Obligations (ARO) Report is to outline the implications of this new standard and present a draft policy. The policy will provide a framework to outline the accounting treatment for ARO so that users of the financial report can discern information about these assets, and their end of life obligations. Councils are legislatively required to adopt such a policy.

**Background:** Recent changes to reporting standards by the Public Sector Accounting Board (PSAB) require municipalities to identify, measure, and report certain costs associated with asset retirement.

Municipalities must prepare an Asset Retirement Obligation Policy that establishes guidelines to ensure compliance with the new standard PSAB PS 3280 – Asset Retirement Obligations. The Treasurer has developed a draft Asset Retirement Obligation Policy for Sub-committee, Committee and Council consideration which has been attached to this report as Appendix A.

The Treasurer will work with Department Heads throughout the year to review all assets owned and controlled by the City against the Asset Retirement Obligation Policy requirements to identify future liabilities. A work plan detailing the activities that must occur has been attached to this report as Appendix B.

The identified liabilities will be measured and included in the City's financial statements beginning in the 2023 fiscal year.

An ARO arises when there is a legal obligation to retire tangible capital assets. Asset retirement is defined as removing a capital asset from service and includes sale transactions, asset abandonment and asset disposal. These costs may include, but are not regularly limited to, decommissioning, dismantling, and remediation of a tangible

capital asset and meeting any legislative mandates around environmental cleanup and/or restoring assets to their original condition.

This exercise has already been undertaken for landfills, specifically under PSAB 3270 Solid Waste Landfill Closure standard, so the City's financial statements already capture these costs and liabilities. The intent of PSAB 3280 - Asset Retirement Obligations is to replace PSAB 3270 and enhance the assets that recognition of retirement obligations to include other assets such as those noted herein.

The exercise of identifying, assessing, and estimating an ARO will require a considerable effort across the City organization and may ultimately require the use of professional consultants. This project will be a significant undertaking for the Finance Division but will also involve the other City divisions as well. It will result in additional work to maintain compliance with the new standard ongoing into the future. Staff have already attended several online training webinars and Finance staff in the neighbouring municipalities in Perth County met to share practices and worked collaboratively to develop this policy.

**Analysis:** The City'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 total 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:

- 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, fuel storage tank removals, wells, fire water holding tanks, septic beds and others.
- Leases that require removal of leasehold improvements at the end of the lease.
- Land covenants needing removing equipment or cleaning up hazardous materials (more comprehensive listings to be determined with reviews of Ministry of the Environment, Conservation and Parks (MECP), Ministry of Natural Resources and Forestry (MNRF), and other legislation, beginning with specific attention to those subject to penalty or fine for failure to comply)
- Assets that need to be returned to their natural state when assets are no longer in use.

Common assets include buildings with asbestos; storage tank removal; removal of radiologically contaminated medical equipment (x-rays or MRI's); wastewater or sewage

treatment facilities; reclamation, closure and post- closure obligations associated with mining activities; closure and post-closure obligations associated with landfills; and reforestation of land subject to a timber lease.

Once an ARO liability is estimated, liability and asset of equal value are recorded on the Statement of Financial Position/Balance Sheet. The initial asset in most cases will already be captured as part of our Tangible Capital Asset registry, and these are part of the Accumulated Surplus. This effectively increases the carrying cost of the existing asset at the same time as registering the liability. Once an asset is no longer in use, then the liability for the ARO will be expensed when the asset is disposed. 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/Income Statement to increase the liability over time as the asset approaches its end of life. 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. Similar to 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 and how it will be funded.

Because the City of Stratford financial statements include consolidated public sector entities (Festival Hydro Inc, Festival Hydro Services Inc, Spruce Lodge and Huron Perth Public Health, the Golf Course, Perth Stratford Housing Corporation and SeedCo/ InvestStratford), this standard will also apply to these entities. Ensuring that these entities appropriately capture asset retirement obligations will also create additional assurance work by staff as well as the auditors.

A new Asset Retirement Obligation Policy was co-developed with the municipalities in Perth to establish the steps to be followed: recognition, subsequent measurement, and staff responsibilities. The draft policy is attached for consideration.

Next steps are outlined on the drafted workplan attached.

## **Financial Implications:**

### **Financial impact to 2023 and future operating budgets:**

It is not anticipated that there will be a significant impact on the City's financial position as a result of recognizing asset retirement obligations. A future report will be prepared for Sub-committee, Committee and Council to outline the assets which have retirement obligations and the estimated costs of the retirement costs. Consideration should be given to creating an Asset Retirement Obligation Reserve to accumulate the necessary funds to cover retirement costs, similarly to that recently established for landfill closure and post-closure costs.

**Link to asset management plan and strategy:**

The City's software used for managing the asset registry (CityWide/Public Sector Digest) does contain a component that will assist with keeping track of the ARO requirements which will make reporting and reviewing once initially established simpler than recreating or managing strictly in Excel or some other system.

As outlined in this report, the total costs of asset ownership and management will increase as the costs of retirement are captured for those identified in the standard.

**Alignment with Strategic Priorities:****Developing our Resources**

Optimizing Stratford's physical assets and digital resources. Planning a sustainable future for Stratford's resources and environment.

**Alignment with One Planet Principles:**

**Not applicable:** This report and outcomes are legislative and administrative in nature and do not align with One Planet principles.

**Staff Recommendations: THAT the draft Asset Retirement Obligation Policy attached to Report FIN23-005, be approved;**

**AND THAT staff be authorized to establish a new Asset Retirement Obligation Reserve Fund if/as required, and this new reserve fund be added to F.1.13 Reserve and Reserve Fund Policy.**

**Prepared by:** Karmen Krueger, CPA, CA, Director of Corporate Services/Treasurer

**Recommended by:** Karmen Krueger, CPA, CA, Director of Corporate Services/Treasurer  
Joan Thomson, Chief Administrative Officer