



**Date:** May 23, 2023  
**To:** Mayor and Council  
**Author:** Ryan McLeod, CPA,CA  
**RE:** 2022 Financial Statements and Year End Review  
**Report No.:** FS-2023-10

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## **RECOMMENDED ACTION**

1. That the Financial Statements for the Corporation of the Town of Kingsville for the year ending December 31, 2022, as audited by BDO Canada LLP, **BE APPROVED**;
2. That the 2022 Treasurer's Statement of Development Charge Reserve Funds, **BE APPROVED**;
3. That By-law 40-2023 to authorize the submission of an application to Ontario Infrastructure Lands Corporation (OILC) for a \$12,000,000 construction loan and the issuance of long-term debt upon completion of the capital works be taken as having been read three times and finally passed and the Mayor and Clerk **BE AUTHORIZED** to sign same;
4. That the 2022 Statement of Investment Activity, **BE APPROVED**; and
5. That the 2022 general budget surplus of \$742,589, be applied to the debt financed balance of the Arena Floor Cooling System Replacement capital project, **BE APPROVED**.

## **BACKGROUND**

As per section 294.1 of the *Municipal Act, 2001*, every year, municipalities are required to prepare financial statements in accordance with Public Sector Accounting Board (PSAB) standards. These statements are required to be audited by an independent accounting firm. Prior to issuing their audit opinion, the Financial Statements must be approved by Council.

In addition to the annual Financial Statements, the Treasurer is also required to provide an annual statement on Development Charge and Investment activities.

The following discussion provides Council with an overview of the 2022 Financial Statements and highlight any significant changes or matters of concern.

## **DISCUSSION**

The Consolidated Financial Statements for the Town of Kingsville reflect all municipal operations, which includes property tax funded and rate funded departments (i.e. Water, Wastewater, and Building). These statements also include the Town's 38.72% share of the Union Water Supply System.

### **Cash and cash equivalents**

On the surface, the Town's cash balance is relatively consistent with 2021, however, this balance includes nearly \$8 million of UWSS cash (2021 – \$4.2 million). The Town's own cash balances have decreased by approx. \$4.2 million from the prior year, which is consistent with the increase in 'Unfinanced Capital' discussed later in this report.

### **Taxes and grants in-lieu receivable**

The Town's tax receivable remains at approximately 4% of total taxes levied which is lower than the regional municipal average of 5.8%, as indicated in 2021 Provincial Financial Indicator Review (Appendix A). A low tax receivable balance is an indicator of effective collection strategies and a healthy local economy.

### **Trade and other receivables**

This refers to water, sewer, and other miscellaneous receivables owing to the Town at year end. The increase over 2022 is primarily attributable to Provincial grants receivable at year end.

### **Drainage costs recoverable**

This refers to drainage work that has yet to be billed. This figure has decreased from 2021 primarily due to the Esseltine Drain project which was billed in Q4 of 2022.

### **Drainage debt receivable**

This refers to drainage work that has been billed, however, the assessed property owners have opted to finance their charges on their tax rolls.

### **Long-term investment**

The 2021 balance referred to Kingsville's share (38.72%) of a \$10,000,000, 5-year GIC, held by Union Water Supply System (UWSS). This investment matured in 2022 and is largely responsible for the increase in the UWSS cash balance at year end.

### **Accounts payable and accrued liabilities**

These accounts tend to fluctuate with the level of capital spending in the final month or two of the year. All vendor invoices are paid upon approval. The Town had no difficulty meeting its financial obligations as they became due throughout the year.

## Municipal debt

A detailed schedule of Municipal Debt can be found in Note 4 of the Financial Statements.

This debt can be summarized in 3 main categories:

	2022	2021	Increase (Decrease)
Property Tax Supported Debt	\$ 5,183,701	\$ 5,899,088	\$ (715,387)
Debt Paid by Benefiting land owners	201,350	314,275	(112,925)
Union Water Debt	3,062,343	3,630,299	(567,956)
	<u>\$8,447,394</u>	<u>\$ 9,843,662</u>	<u>\$ (1,396,268)</u>

The only component of the Municipal Debt noted above which Council has direct control over is the “Property Tax Supported Debt”. This figure is driven by the decisions Council makes during budget deliberations.

It is important to note the Debt reported on the Financial Statements does not include unfinanced capital. Unfinanced capital refers to amounts which the Town is internally financing through reserves, but will eventually recover through the future issuance of long-term debt or other funding sources. At December 31, 2022, the Town’s Unfinanced Capital balance consisted of the following;

	2022	2021	Increase (Decrease)
Wastewater Projects (Rate funded)	\$ 20,251	\$ 20,251	\$ -
Road 2 E (Tax funded)	462,149	593,749	(131,600)
Lakeshore East Sewer (DC Funded)	309,537	309,537	-
Road 2 E (DC Funded)	1,437,442	-	1,437,442
SW Water Supply (DC funded)	3,579,171	708,783	2,870,388
	<u>\$5,808,550</u>	<u>\$1,632,320</u>	<u>\$ 4,176,230</u>

Based on the unfinanced capital balances noted above, and the capital works approved in the 2023 budget, Administration recommends that Council approve a by-law to authorize a \$12,000,000 construction loan with Ontario Infrastructure and Lands Corporation (OILC) to finance the Development Charge (DC) component of the Road 2 E road reconstruction and southwest water supply expansion.

At the time of this report, Construction loans from OILC bear interest at 5%. When these projects are complete, Administration is proposing to finance the road component over a 10 year period and the water component over a 20 year period. The Town is well within its Annual Repayment Limit, as calculated by the Province, to support this level of debt.

## Employee future benefits

The Employee Future Benefit Obligation represents the Town's estimated liability for benefit payments for its current and future retirees. This benefit is provided to employees who retire earlier than age 65 and is ended when the retired employee has their 65<sup>th</sup> birthday.

In 2022, the Town obtained an updated valuation report which identified significant actuarial gains, reducing the Town's estimated liability by \$737,700. This gain is driven primarily by lower than expected premium rates and other plan experience factors.

For clarity, the Employee Future Benefit obligation refers to post retirement benefits only, and is completely separate from the employee pension plan managed by OMERS. As of December 31, 2022, the Town has fully funded the employer contributions required under the OMERS pension plan.

## Deferred revenue

Deferred Revenue consists of the following;

	2022	2021	Increase (Decrease)
Development Charges	\$ 44,640	\$ 98,199	\$ (53,559)
Unspent Grants	2,302,394	3,875,255	(1,572,861)
	<u>\$ 2,347,034</u>	<u>\$ 3,973,454</u>	<u>\$ (1,626,420)</u>

During 2022 the Town collected \$2,426,759 in Development Charges (DC). These funds are collected upon the issuance of building permits and are held in a reserve to finance various growth related capital projects. Over the past 2 years, the Town proceeded with several large scale DC projects, namely the Road 2 E reconstruction, the Southwest water supply and the Cottam Lagoon expansion, which has significantly reduced DC reserve balances. As discussed in the Municipal Debt section of this report, some of the Town's Development Charge projects which are currently underway, will need to be debt financed and repaid through the future collection of DCs.

Please refer to Appendix B for the Treasurer's Annual Statement of Development Charge Activity for full details.

## Tangible capital assets

Tangible capital assets refers to all of the infrastructure, property, and equipment owned by the Town. This includes assets that were purchased directly by the Town and infrastructure that have been contributed to the Town from developers. It is important to note that the value reported on the financial statements refers to historical cost, less accumulated amortization (also known as "Book Value"), which is significantly lower than replacement value.

Replacement Value of “Core Assets” per Asset Management Plan	\$613 million
Book Value of Capital Assets per Financial Statements	<u>\$160 million</u>
Difference	\$453 million

Council should rely on its Asset Management Plan and other infrastructure studies for long-term financial planning with respect to tangible capital assets. Administration will bring an updated Asset Management Plan to Council later this year.

### Annual surplus

The Consolidated Statement of Financial Operations and Accumulated Surplus, also known as an “Income Statement”, can be found on page 4 of Financial Statements. This statement provides a summary of the financial activities of the Town for the year ended December 31, 2022.

Under PSAB, the Town is reporting a surplus of \$17,151,230 for 2022. This surplus includes \$5.6M in contributed capital from private developers and \$2.4M from its share of UWSS.

It is important to note there are a number of significant differences between PSAB standards and the modified cash based / fund accounting methods used by the Town for budgeting purposes. The most significant differences between these two methods of accounting are as follows;

	PSAB	Budget Accounting
Capital Assets	Most capital expenditures are recognized on the Balance Sheet as long-lived assets and amortized over their useful lives	Capital expenditures are treated as an expense in the year incurred.
Developer Contributions	Any assets built and transferred to the Town are considered to be income at the time of transfer.	Developer contributions are not budgeted for.
Long-term Debt Repayments	Only the interest portion of long-term debt repayments is an expense.	Both the principle and interest payments are expensed in the year incurred.
Reserves	Reserve activity is neither recognized as ‘revenue’ or an ‘expense’	Contributions from reserves are recognized as revenue, contributions to reserves are considered to be an expense.
Employee Future Benefit Obligation	An actuarial valuation is performed. The estimated obligation is recognized as a liability on the Balance Sheet.	Benefit payments on behalf of retirees are expensed in the year the payments are made.

Water & Wastewater & Building Depts.	The Financial Statements include all of the Town's water, wastewater and building department activities.	For budgeting purposes, each of these operations have separate stand-alone budgets.
Union Water Supply System	The Financial Statements include the Town's proportionate share of UWSS assets, liabilities and annual surplus / deficit	The UWSS budget is not incorporated into the Town's budget.

For budget purposes, the Town is reporting a general surplus of \$742,589 from 'tax funded' operations. Please refer to Appendix C for a detailed reconciliation of the surplus for budget purposes to the surplus reported under PSAB standards.

For perspective, this general budget surplus equates to 2.5% of the Town's Operating and Capital expenses during the year.

This surplus is primarily the result of the following:

- Staffing vacancies and leaves of absence resulted in wages and benefit savings of approximately \$385,000
- Higher than expected 'Supplement Tax Revenue' from in-year MPAC assessments contributed to additional \$300,000 in revenue.

### **Budget Surplus Allocation**

During 2023 Budget deliberations, Council approved a project to replace the in-floor cooling system and boards are the Arena. The Budget for this project was \$1.8 million and funded as follows;

Reserves	\$600,000
Taxation	\$300,000
Debt	<u>\$900,000</u>
Total	\$1,800,000

Administration recommends applying the 2022 surplus against the "debt" financed portion of this project. This will reduce pressure on future tax rate increases and put the Town in a better financial position to respond to other facility needs.

### **Union Water Supply System (UWSS)**

The PSAB financial statements include our proportionate share of UWSS assets, liabilities and any surplus or deficit. As of December 31, 2022 the Town's ownership in UWSS was 38.72%.

The Town's share of UWSS Surplus in 2022 was \$2,382,090. Please refer to Note 3 of the Financial Statements for a breakdown of how UWSS is consolidated with the Town's Financial Statements.

## **Investment Income**

In Ontario, a municipality's ability to invest surplus funds is heavily regulated by O. Reg. 438/97. In addition to compliance with statutory requirements, the Town's Cash Management and Investment Policy, cites the *Preservation of Principle* and *Maintaining Liquidity* as key investment objectives.

During 2022, the Town benefited from a general rise in interest rates. Between term deposits and interest on savings accounts, the Town earned \$561,343 (2021 - \$251,983) of investment income in 2022. Please refer to Appendix D for a schedule of the Town's financial security activities for the year. All investments are consistent with the Town's Cash Management and Investment policy.

## **Reserves**

As discussed above, Reserves are neither an asset nor a liability under PSAB financial reporting, they are simply an internal allocation of equity. Page 21 of the Financial Statements includes summary of the Town's reserve balances at year end. In 2022, the Town's overall reserve balance increased by approx. \$2.8 million. Based on the Provincial Financial Indicator review, the Town's reserve balances in relation to operating expenses are slightly 'above average' for Southern Ontario lower-tier municipalities, however, this metric can change quickly based on the timing of large capital expenditures.

## **FINANCIAL CONSIDERATIONS**

Overall, the 2022 Financial Statements indicate that the Town is in a relatively healthy financial position. However, it is important to understand that Financial Statements report transactions which have already occurred and do not project the future.

Most importantly, these statements do not provide a commentary on the current state of the Town's infrastructure, nor do they disclose any financial requirements to replace or maintain infrastructure in the future. For the Town to maintain a healthy financial position over the long-term, it is imperative for Council commit to closing its infrastructure funding gap through steady annual increases in infrastructure funding.

Although existing debt levels are relatively low today, Council should expect these levels to rise as the Town completes the Road 2 E project, Westside Collector Road and other key infrastructure projects.

## CAO Comments

The CAO is concerned that recent changes in provincial legislation, namely Bill 23, suggest that the Town may be required to forego development charges for some housing developments which meet an “attainable” or “affordable” criteria. The province has not issued regulations and there is significant uncertainty how this legislation will impact the Town. The issuance of future debt to cover needed infrastructure expenditures is concerning if the Town cannot rely on the payment of expected development charge revenue to pay back this debt.

## ENVIRONMENTAL CONSIDERATIONS

There are no direct environmental considerations associated with this report.

## CONSULTATIONS

Financial Services Team

PREPARED BY:



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REVIEWED BY:



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