

<b>TO:</b>	<b>CHAIR AND MEMBERS CORPORATE SERVICES COMMITTEE MEETING ON JULY 17, 2018</b>
<b>FROM:</b>	<b>ANNA LISA BARBON MANAGING DIRECTOR, CORPORATE SERVICES AND CITY TREASURER, CHIEF FINANCIAL OFFICER</b>
<b>SUBJECT:</b>	<b>RESERVE &amp; RESERVE FUND POLICY REPORT</b>

**RECOMMENDATION**

That on the recommendation of the Managing Director, Corporate Services and City Treasurer, Chief Financial Officer the attached proposed by-law (Appendix A) **BE INTRODUCED** at the Municipal Council meeting on July 24, 2018 to enact a Reserve and Reserve Fund Policy.

**PREVIOUS REPORTS PERTINENT TO THIS MATTER**

Corporate Services Committee, May 29, 2018, Agenda Item #2.2, 2018 Reserve Fund Housekeeping Report

**LINK TO 2015-2019 STRATEGIC PLAN**

Council's 2015-2019 Strategic Plan for the City of London identifies "Leading in Public Service" as one of four strategic areas of focus. The Reserve & Reserve Fund Policy Report supports this strategic area of focus by contributing towards the strategic priority "Proactive financial management".

**BACKGROUND**

The purpose of this report is to seek Council approval of a Reserve and Reserve Fund Policy (the "Policy"). The Policy has been developed to formalize the standards to which the Corporation of the City of London (the "City") manages reserves and reserve funds, educate internal and external stakeholders regarding the practices applied and to provide transparency, accountability and opportunities for engagement.

This Policy was also developed through a robust evaluation and research period which included:

- A thorough review of senior government requirements,
- Internal consultations with service areas which rely on reserves and reserve funds as a part of their operations,
- External consultations with comparable Ontario municipalities that have implemented a reserve and reserve fund policy, and
- Best practice research from public associations such as the Municipal Finance Officers Association of Ontario (MFOA) and the Government Finance Officers Association (GFOA).

Reserves and reserve funds are an important element of the City's long-term strategic financial plan as they allow the City to set aside funds for known and unknown future events. Examples of future events include, but are not limited to: provisions for the replacement and rehabilitation of existing assets, funds for new capital assets, funding long-term contingencies and potential liabilities and providing a buffer for significant unanticipated expenditures or loss of revenues beyond the control of the City. They also minimize fluctuations in taxes caused by cyclical conditions.

Two additional factors to consider when rationalizing reserves and reserve funds are the City's credit rating and intergenerational equity. Credit rating agencies assess the appropriateness of corporations' reserve and reserve fund balances when setting credit ratings. Thus the establishment of a well-structured reserve and reserve fund portfolio keeps the City in a strong financial position and contributes to the maintenance of the City's Aaa credit rating which reduces the cost to borrow money. Intergenerational equity is the concept of fairness between generations (pay now or pay later). Reserves and reserve funds support the objective of intergenerational

equity by setting aside funds now, equal to current ratepayers' usage/benefit, to pay for costs that are going to occur in the future. An example of this concept is saving for the future replacement or rehabilitation costs of a community centre; the generation benefiting from the use of the asset is the same generation contributing to the savings that will help replace or rehabilitate the asset. When this approach is not taken, the burden to pay is passed to future generations who did not receive the benefits of the cost they are asked to bear.

The potential consequences of not having adequate reserve and reserve fund levels are:

- **Increased cost of short-term borrowing** - A lack of sufficient reserves and reserve funds available to meet operational needs may require the City to potentially seek short-term financing from external sources at an increased cost to the City.
- **Loss of Aaa credit rating** - Moody's, the City's credit rating agency, has outlined that improving reserve and reserve fund levels assist the City in achieving its credit rating. A drop in this rating would increase the overall cost of borrowing resulting in a direct impact to the City's operating & capital (growth) budgets.
- **Reduction in capital plan** - Reserve and reserve fund balances assist in financing the capital plan of the City. A reduction in balances would require the City to reduce the capital plan, if all else remained equal.
- **Improper intergenerational equity** - By not setting aside funds now to pay for costs that are going to occur in the future (examples include unfunded liabilities and capital asset renewal and replacement), the burden to pay is passed to future generations who did not receive the benefits of the cost.

For the purpose of this Policy reserves and reserve funds are defined as follows:

**Reserve:** An appropriation from net revenue and/or cost savings at the discretion of Council, after the provision for all known expenditures. It has no reference to any specific asset and does not require the physical segregation of money or assets as in the case of a reserve fund. Council may set up reserves for any purpose for which they have the authority to spend money and they are generally used to mitigate the impact of fluctuations in operating costs and revenues. Reserves do not earn interest as balances held in reserves form part of the general cash balances managed by the City. All reserves are "discretionary", being those set up by Council. Examples of reserves currently used to mitigate budgetary fluctuations include: Operating Budget Contingency Reserve, Wastewater Rate Stabilization Reserve and Unfunded Liability Reserve.

**Reserve Fund:** Funds that have been set aside by a by-law of the City. As a result, reserve funds are either "discretionary", being those set up by Council or "obligatory", being those set up by virtue of senior government statute or agreement. The use of reserve funds is restricted to a specific purpose. Reserve fund balances are segregated from general cash balances managed by the City. They earn interest and earnings are proportionally applied to each reserve fund based on yields earned on the City's total investment portfolio and cash balances. Council may set up reserve funds for any purpose for which they have the authority to spend money. Examples of reserve funds include: City Facilities Reserve Fund, Economic Development Reserve Fund and Waterworks Reserve Fund.

As demonstrated in past budgets and reports, the City has developed, implemented and maintained, a collection of reserves and reserve funds that align with the context of reserves and reserve funds stated above. Through the accompanying Policy, these practices will be clearly documented and formalized. Upon approval of this Policy, administration will undertake efforts over the next twelve to eighteen months to rationalize the City's reserve and reserve fund portfolios. This will include an evaluation of the appropriateness of each reserve and reserve fund, an evaluation of the guiding documents (resolutions, by-laws, etc.) of each reserve and reserve fund as well as recommendations of targets for each. This effort has already commenced with a report on the City's reserves expected to be presented to Council in August 2018. This will be followed by a similar report in 2019 on the City's reserve funds. The exact timing of this future report will be better known as efforts to complete the City's 2019 DC Background Study and 2018 Corporate Asset Management Plan progress. Each of these milestone reports informs the evaluation and target setting efforts for the respective reserve funds that support the infrastructure addressed in each report.

<b>THE POLICY</b>
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The Policy provides for the management and administration of reserves and reserve funds. The following summarizes the guiding principles, objectives, management practices and standard of care contained within the Policy.

## Principles

The principles of the Policy center around why the City should maintain adequate reserves and reserve funds (liquidity, intergenerational equity, credit rating and cost of borrowing), what types must exist and their level of integration into the budget and strategic financial plan.

The factors of liquidity, intergenerational equity, credit rating and cost of borrowing provide evidence as to why the maintenance of reserves and reserve funds is so important.

- **Liquidity:** Without sufficient savings for expenses such as the replacement and rehabilitation of capital assets, long-term contingencies and potential liabilities and other known and unknown events, the City faces the prospect of not being able to meet its financial obligations due to cash flow constraints.
- **Intergenerational Equity:** Helps formulate when and how much should be contributed to reserve and reserve fund balances to ensure a reasonable amount of parity across societal generations.
- **Credit Rating:** The City's credit rating and cost of borrowing move in opposite directions depending on, among other things, the level of reserve and reserve fund balances the City holds. This helps to understand and justify present and future reserve and reserve fund balances.

The two **types of reserves and reserve funds** the City maintains to support its budgets are obligatory and discretionary. The obligatory type relates only to reserve funds; created when a senior government statute or agreement requires that revenue received for special purposes be segregated from the general revenues of the municipality. Thus obligatory reserve funds are to be used solely for the purpose prescribed for them by statute or agreement. The discretionary type relates to both reserves and reserve funds; created by Council to set aside revenue and/or cost savings to finance a future expenditure for which Council has the authority to spend money. This means the discretionary reserves and reserve funds created can help to finance any service/program within Council's purview.

Finally, the principles of the Policy mandate that reserves and reserve funds form an integral component of the City's **budget and strategic financial plan**. The purpose of this principle is to connect all the reserves or reserve funds created and managed by the City with the objectives of the operating and capital budgets and the long-term strategic financial plan. This principle ensures no reserve or reserve fund is created without purpose and are in support of the long-term goals of the municipality.

## Objectives

The objectives of the Policy are to provide adherence to statutory requirements, promote financial stability and flexibility, save for major capital expenditures and reduce tax/rate supported debt.

**Adherence to statutory requirements** specifies that all reserve and reserve funds managed by the City shall be established and managed in accordance with senior government statutory requirements. Statutory requirements include controls relating to reserve and reserve funds such as Council's authority in passing by-laws, what information the budget shall include, reporting requirements and the segregation and investment of reserve fund balances, to name a few. By following each of these standards, the City will achieve a high degree of control over reserves and reserve funds under its authority.

**Promotion of financial stability and flexibility** focuses on the need to maintain adequate reserve and reserve fund levels in line with public sector best practices to achieve long-term financial success. To support the fulfillment of this objective, the Policy mandates the following categories of reserves and reserve funds be used:

- Obligatory,
- Capital Asset Renewal and Replacement,
- Capital Asset Growth,
- Special Projects and New Initiatives, and
- Contingencies/Stabilization and Risk Management.

Each category relates to a different purpose for which a reserve or reserve fund is created. For example, reserve funds categorized as capital asset renewal and replacement are established to save for future capital costs of existing assets. Reserve funds categorized as capital asset growth are established to save for future capital costs of new assets. Combining reserves and reserve funds into categories facilitates the establishment, monitoring and reporting of balances.

**Saving for major capital expenditures** is one of the primary uses of reserves and reserve funds. As such, the Policy includes parameters in regards to the City's budgeting for capital asset renewal and replacement (existing assets) and capital asset growth (new assets) reserve funds. When saving for existing assets, contributions to reserve funds should commence in either the fiscal year the asset is acquired or put into service. Guidance suggests the annual amount contributed should represent the full future cost of replacement or rehabilitation, divided by either the estimated useful life of the asset or the consumption rate of the asset by current ratepayers. This approach ensures that at a minimum the historic cost of the asset is reflected when budgeting for contributions and that the principle of intergenerational equity is considered. Contributions for new assets are significantly different as they are based on both developer and ratepayer contributions. Developer contributions come in the form of development charge (DC) levies and relate to the growth component of new capital assets. Ratepayer contributions come from tax/rate funding sources (examples include capital levy, water rates and discretionary reserve funds) to support the non-growth component which benefits existing ratepayers. DC levies collected are deposited in the City's obligatory reserve funds, which are restricted to funding growth components of future capital works. The tax/rate funding sources are drawn in the year in which the capital works commence. If the growth component of future capital works exceeds the balances in the growth related obligatory reserve funds, debt may be issued in accordance with the *Development Charges Act, 1997, as amended*, and other pertinent City policies.

**Reducing tax/rate supported debt** is another primary use of reserves and reserve funds. Without these savings the City would face significant swings in either the tax supported capital levy, or debt required to support the capital budget. Thus through the use of reserves and reserve funds the City can minimize the need for debt as a source of financing within the capital budget. Reserves and reserve funds are a significant portion of the financing contained within the City's capital budget. Furthermore, the Policy permits Civic Administration to use reserve and reserve fund balances as a source of debt substitution in the capital budget when appropriate. Determining whether the option is appropriate includes consideration of the reserve and reserve fund balance, future commitments and the criteria of the reserve or reserve fund being considered given the nature of the capital work to be funded. Should reserve and reserve fund balances be used for debt substitution, the City Treasurer has the authority to reallocate the future debt servicing cost savings to reserves and reserve funds that are below established targets. It being noted that such contributions are subject to Council approval through the City's budget process.

### **Reserve and Reserve Fund Management**

This section provides for the operational procedures and practices required for the prudent management of reserves and reserve funds held by the City. These procedures and practices include the establishment and modification of reserves and reserve funds, the investment of balances held, authority and reporting over contributions to/drawdowns from, lending/temporary borrowing and the steps for termination. Review and consideration of each of these duties is important as they represent the routine functions performed in the management of reserves and reserve funds.

When **establishing and modifying reserves and reserve funds** a supporting financial plan must be in place. Financial plans should identify the funding needs the reserve or reserve fund is proposed to support, the target balance to be maintained, what the projected contributions to/drawdowns from are and the investment standards to be applied.

The method for assessing and determining a responsible target balance varies on a case-by-case basis due to the broad spectrum of funding needs reserves and reserve funds support. Although there can be significant differences in the ways targets are calculated, Civic Administration, at a minimum, will consider the following when formulating targets:

- Purpose of fund,
- Certainty of end needs,
- Best practices/standards available, and
- Economic factors.

After targets have been established, reserve and reserve fund balances and targets should be periodically reviewed to ensure they are adequate over the 10 year budget period.

The gross amount of the City's holdings in reserves and reserve funds is significant due to the size and complexity of its operations. Thus it is prudent that a reasonable share of the City's **balances held be invested** in accordance with the Investment Policy to earn a competitive rate of return. The rules applied to the investment of reserves and reserve funds are:

- Funds shall be invested for a term that will not exceed its expected date of need;
- Interest earned on reserves shall be recognized as revenue in the operating budget; and

- Interest earned on reserve funds shall be recognized as revenue in each specific reserve fund according to its proportionate share of the investment portfolio.

Once Council has approved the establishment of a reserve or reserve fund, contributions to/drawdowns from take place to meet the identified needs and target. **Authority over contributions to/drawdowns from** reserve and reserve funds is governed by the applicable resolution or by-law and this Policy. The majority of contributions to/drawdowns from are approved by Council as part of the multi-year budget and annual budget update processes, or specifically by resolution for occurrences that fall outside of the budget process. The exceptions to this rule relate to administrative authority provided by Council approved by-laws, examples of which are direct contributions such as development charge revenue, contributions to/drawdowns from made under the authority of the Surplus/Deficit Policy and the use of revolving reserve and reserve funds such as the Workplace Safety and Insurance Board Reserve Fund. Any previously approved contributions to/drawdowns from not realized are reported to Council as part of the mid-year and year-end budget monitoring reports, or budget process.

If sufficient balances exist within the City's reserves and reserve funds portfolio, **intra-fund lending and external loans** are permitted. Having the flexibility to lend/temporarily borrow across reserves and reserve funds helps to avoid the cost of cash flow deficiencies, reduces the cost of borrowing and minimizes the administrative effort required to coordinate financing.

Intra-fund lending is the temporary borrowing amongst the reserves and reserve funds managed by the City. For this form of lending, discretionary reserves and reserve funds can lend and borrow between each other with no limits, but discretionary accounts cannot borrow from obligatory reserve funds, they can only lend to them. This limitation relates to the *Development Charges Act, 1997, as amended*, which prohibits the loaning of obligatory reserve funds. All transfers (discretionary to discretionary, discretionary to obligatory and obligatory to obligatory) must bear the City's internal rate of return and principal and interest are to be credited to the reserve or reserve fund that sourced the transfer.

External loans relate to Council approved loans that meet the requirements of Section 107 of the *Municipal Act, 2001, as amended*. Section 107 gives Council the authority to make grants, to any person, group, or body for any purpose considered to be in the best interest of the municipality. When recommending such loans to Council, Civic Administration shall consider the following:

- External loans shall only be made to public agencies/groups and shall benefit the public;
- The term of external loans shall not exceed five years;
- Appropriate security shall be provided to protect the interests of the City;
- A financial profile of the borrower;
- Whether adequate reserves and reserve funds are available for the term of the external loan; and
- What rate shall the external loan bear and that principal and interest shall be credited to the appropriate reserve or reserve fund source.

As noted above, all external loans shall be provided from discretionary reserves and reserve funds as the external lending of obligatory reserve funds is prohibited.

Lastly, **termination of reserves and reserve funds** shall be considered when the program or project it supports is no longer in the scope of the City's strategic plans, commitments have been completed and no future commitments are expected and administration is confident the balances in other reserves/reserve funds can mitigate the need to hold any remaining balance. Reserves or reserve funds identified for termination shall be reported to Council for review and approval with recommendations regarding timing and reallocation of remaining balances.

### **Standard of Care**

The Standard of Care section of the Policy covers the delegation of authority assigned to the City Treasurer over reserve and reserve funds managed by the City, the reporting requirements the City Treasurer is obligated to meet and when Policy reviews and updates are to occur.

**Delegation of authority** within the Policy clearly outlines when and what authority over reserves and reserve funds is transferred from Council to the City Treasurer and from the City Treasurer to a designate. The delegations provided for in the Policy include:

- Once Council approves reserves by resolution and reserve funds by by-law, the City Treasurer shall have overall authority for the reserves and reserve funds managed by the City;
- The City Treasurer may delegate management authority over the reserves and reserve funds managed by the City to a designate;
- The City Treasurer, or designate has the responsibility for setting reserve and reserve fund

targets, it being noted targets will be periodically reported to Council through reserve and reserve fund reports; and

- The City Treasurer, or designate shall have overall responsibility for this Policy, and the authority to implement a program for reserves and reserve funds and establish procedures consistent with the content of this Policy.

These delegations provide for appropriate transfers of power when needed and allow for the effective and efficient management of reserves and reserve funds.

There are several points at which Civic Administration must report on reserve and reserve fund balances. The **reporting requirements** contained within the Policy cover each of them as well as opportunities for other reports to be brought forward. The reports the City Treasurer or designate are to prepare include:

- Annual Audited Financial Statements - the annual audited financial statements include a statement of financial position, financial activities and changes in fund balances for reserves and reserve funds.
- Reserve and Reserve Fund Report - a financial plan forecasting reserve and reserve fund balances and a comparison to target objectives will be prepared periodically based on the most current information available; this report may include the establishment of new, modification of existing and termination of existing reserves and reserve funds.
- Budget Reports - reserve and reserve fund balances, projected contributions, and planned drawdowns for a ten year period are to be presented in each multi-year budget, and annual changes to reserve and reserve fund balances shall be presented with each annual budget update or specifically by resolution if required.
- DC Reserve Funds Report - an annual report detailing pertinent information regarding DC reserve funds shall be presented to Council as required by the *Development Charges Act, 1997, as amended*.
- Other reports in line with this Policy shall be brought forward to Council as required.

These reports provide for the transparent reporting of reserves and reserve funds, help to educate internal and external stakeholders, fulfill legislative reporting requirements and facilitate ongoing monitoring and continuous improvement.

**Policy reviews** and updates are to occur every four years, in the first year of each elected Council, if there are any amendments required. In addition, the Policy allows for Council or the City Treasurer to bring forward reviews and updates outside of this period as deemed necessary. These guidelines provide flexibility so the Policy can be updated frequently to reflect changes in senior government legislation/requirements, best practices and other potential changes impacting reserves and reserve funds.

<b>CONCLUSION</b>
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Reserves and reserve funds are an important element of the City's long-term strategic financial plan. The attached by-law and Policy (Appendix A) sets a framework for the management of reserves and reserve funds which includes guiding principles, primary objectives, key management and administrative responsibilities and standards of care for reserves and reserve funds managed by the City. These standards will help to further develop, implement and monitor a reserve and reserve fund portfolio that meets the City's changing needs while providing accountability and transparency for the use of public funds. Therefore, Civic Administration is recommending approval of the Reserve and Reserve Fund Policy.

This report was prepared with the assistance of Alan Dunbar, Financial Planning and Policy.

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## APPENDIX A

Bill No.  
2018

By-law No. CPOL.-

A by-law to adopt a new Council Policy entitled Reserve and Reserve Fund Policy.

WHEREAS section 5(3) of the *Municipal Act, 2001*, S.O. 2001, C.25, as amended, provides that a municipal power shall be exercised by by-law;

AND WHEREAS section 9 of the *Municipal Act, 2001*, S.O. 2001, C.25, as amended, provides a municipality with the capacity, rights, powers and privileges of a natural person for the purpose of exercising its authority;

AND WHEREAS the Council of The Corporation of the City of London wishes to adopt a new Council policy entitled Reserve and Reserve Fund Policy;

NOW THEREFORE the Municipal Council of The Corporation of the City of London enacts as follows:

1. The policy entitled "Reserve and Reserve Fund Policy", attached hereto as Schedule "A", is hereby adopted.

2. This by-law shall come into force and effect on the date it is passed.

PASSED in Open Council on July 24, 2018.

Matt Brown  
Mayor

Catharine Saunders  
City Clerk

First Reading – July 24, 2018  
Second Reading – July 24, 2018  
Third Reading – July 24, 2018



## SCHEDULE “A”

**Policy Name:** Reserve and Reserve Fund Policy

**Legislative History:**

**Last Review Date:** July 17, 2018

**Service Area Lead:** Managing Director, Corporate Services and City Treasurer, Chief Financial Officer

### 1. Policy Statement

A Policy governing the management and administration of reserves and reserve funds.

The purpose of the Policy is to establish guiding principles, primary objectives, key management and administrative responsibilities, and standards of care for reserves and reserve funds managed by the City.

### 2. Definitions

- 2.1. **Budget:** An estimated financial plan of revenue and expenditure for a set period of time.
- 2.2. **Capital Asset Renewal & Replacement:** A category of reserve funds established to provide funding for the repair and maintenance of existing City assets to ensure city-owned assets do not deteriorate over time.
- 2.3. **Capital Asset Growth:** A category of reserve funds established to provide funding to new capital initiatives while allowing the City to stabilize the cost of purchasing major capital assets by spreading the cost over multiple years.
- 2.4. **City:** The Corporation of the City of London.
- 2.5. **City Treasurer:** The individual appointed by the municipality as treasurer.
- 2.6. **Contingencies/Stabilization & Risk Management:** A category of reserves and reserve funds designed to fund future obligations which are based on calculated estimates and to mitigate unforeseen events or one-time unanticipated revenue losses and expenses.
- 2.7. **Debt:** Any obligation for the payment of money. For Ontario municipalities, debt would normally consist of debentures as well as either notes or cash from financial institutions, but could also include loans from discretionary reserves and reserve funds.
- 2.8. **Development Charges Background Study:** The background study undertaken by the City for its current Development Charges By-law.
- 2.9. **Discretionary Reserves and Reserve Funds:** A reserve or reserve fund created by Council to set aside revenue to finance a future expenditure for which Council has the authority to spend money.
- 2.10. **GFOA:** Refers to the Government Finance Officers Association of the United States and Canada, a professional association of state, provincial and local finance officers dedicated to the sound management of financial resources.
- 2.11. **Intergenerational Equity:** In economic, psychological, and sociological contexts, is the concept or idea of fairness or justice between generations.
- 2.12. **Liquidity:** A measure of an asset’s convertibility to cash.

- 2.13. **MFOA:** Refers to Municipal Finance Officers Association of Ontario, a professional association which promotes the interests of its members in carrying out their statutory and financial responsibilities by initiating studies and sponsoring seminars to review, discuss and develop positions on important policy and financial management issues.
- 2.14. **Obligatory Reserve Funds:** A reserve fund created when senior government statute or agreement requires that revenue received for special purposes be segregated from the general revenues of the municipality. Obligatory reserve funds are to be used solely for the purpose prescribed for them by statute or agreement.
- 2.15. **PSAB:** Refers to the Public Sector Accounting Board, an independent board with the authority to set accounting standards for the public sector.
- 2.16. **Reserve:** An appropriation from net revenue and/or cost savings at the discretion of Council, after the provision for all known expenditures. It has no reference to any specific asset and does not require the physical segregation of money or assets as in the case of a reserve fund. Municipal Councils may set up reserves for any purpose for which they have the authority to spend money.
- 2.17. **Reserve Fund:** Funds that have been set aside either by a by-law of the municipality or by a requirement of senior government statute or agreement to meet a future event. As a result, reserve funds are either “discretionary” being those set up by Council, or “obligatory” being those set up by virtue of a requirement of senior government statute or agreement. Municipal councils may set up reserve funds for any purpose for which they have the authority to spend money.
- 2.18. **Revolving Reserves and Reserve Funds:** Reserves and reserve funds used to fund normal course operating requirements or cash flow deficiencies that do not require Council approval provided they conform with intent of originating resolution or by-law.
- 2.19. **Specific Projects & New Initiatives:** A category of reserves and reserve funds established for planned savings within the budget to fund projects or expenses either identified at the time the reserve or reserve fund is set-up or after, which allows the City to save for planned or unanticipated projects or expenses that may arise and do not have another funding source.

### 3. **Applicability**

This Policy applies to all reserves and reserve funds administered by the City, including those administered for any of the City’s Local Boards, Commissions, Agencies, or Corporations.

Furthermore, the Policy applies to all City employees who are responsible for the establishment, monitoring, administration and management of the City’s reserves and reserve funds.

### 4. **The Policy**

#### 4.1. **Principles & Objectives**

The guiding principles for reserves and reserve funds shall be:

- a) **Budget and Strategic Financial Plan** - Reserves and reserve funds shall form an integral component of the City’s budget and strategic financial plan.

- b) Liquidity** - Reserves and reserve funds shall be kept at an adequate level to ensure the City has sufficient cash flow to meet its financial obligations; including but not limited to:
- i) Replace and rehabilitate capital infrastructure assets as required;
  - ii) Supply funds for new capital assets identified in the City's long-term plans, or that arise from time-to-time;
  - iii) Fund long-term contingencies and potential liabilities; and
  - iv) Provide a buffer for significant unanticipated expenditures, or loss of revenues beyond the control of the City.
- c) Intergenerational Equity** - Reserve and reserve fund balances shall be maintained to support the principle of intergenerational equity whereby the generation of citizens who benefit from an investment are also responsible for financing it to the greatest extent possible.
- d) Credit Rating and Cost of Borrowing** - Reserve and reserve fund balances impact the City's credit rating and associated cost of borrowing thus at a minimum, reserve and reserve fund balances shall be maintained at levels that support the maintenance of the City's credit rating awarded by Bond Rating Agencies.
- e) Reserve and Reserve Fund Types** - the type of reserves and reserve funds the City shall maintain are as follows:
- i) *Obligatory* - A *reserve fund* created when a senior government statute and/or agreement requires that revenue received for special purposes be segregated from the general revenues of the municipality. Obligatory reserve funds are to be used solely for the purpose prescribed for them by statute or agreement.
  - ii) *Discretionary* - A *reserve or reserve fund* created by Council to set aside revenue and/or cost savings to finance a future expenditure for which Council has the authority to spend money.

The primary objectives for reserves and reserve funds shall be in priority order:

- f) Adherence to Statutory Requirements**
- i) It shall be the City's practice to establish and maintain segregated reserve funds that meet all statutory obligations.
  - ii) Reserves and reserve funds shall be managed in accordance with the *Municipal Act, 2001, as amended*, this includes:
    - Section 10 (2) authorizing single-tier municipalities to pass by-laws respecting accountability, transparency and financial management;
    - Section 290 (2) the budget shall set out the estimated revenues and expenditures of reserves and reserve funds contained within a municipalities budget;
    - Section 291 covering multi-year budget requirements of municipalities;
    - Section 417 (4) that money raised for a reserve fund shall be paid into a special account and shall be invested only in securities or classes of securities prescribed;
    - Section 418 (3) as allowed by the Corporation, shall combine money held in any fund (including General, Capital and Reserves and Reserve Funds) for investment purposes; and
    - Section 418 (4) that earnings from combined investments shall be credited to each segregated fund in proportion to the amount invested in it.
  - iii) Reserves shall be established by Council resolution which governs the purpose, funding sources, and drawdowns of the fund.
  - iv) Reserve funds shall be established by Council by-law which governs the purpose, funding sources, drawdowns, and investment of the fund.

**g) Promotion of Financial Stability and Flexibility**

- i) It shall be the City's practice to maintain adequate reserves and reserve funds within the following categories to achieve long-term financial stability and flexibility (see definitions for detailed description of categories):
  - Obligatory,
  - Capital Asset Renewal and Replacement,
  - Capital Asset Growth,
  - Special Projects and New Initiatives, and
  - Contingencies/Stabilization and Risk Management.
- ii) The City shall strive to maintain reserve and reserve fund levels in line with public service associations best practices (Municipal Finance Officers Association (MFOA), Government Finance Officers Association (GFOA), Public Sector Accounting Board (PSAB), etc.), bond rating agencies standards and other municipalities with comparable credit ratings.

**h) Provision for Major Capital Expenditures**

- i) It shall be the City's goal to maintain adequate reserves and reserve funds to replace and rehabilitate major capital assets, as required, and to provide for new capital assets that have been identified in the long-term capital plan. To achieve this goal, the following budget practices will be applied where applicable:
  - Reserve funds for the full cost of replacement or rehabilitation of major assets will be funded from ongoing operations at a rate which reflects the consumption of that asset by current ratepayers. Contributions to these funds will commence in the fiscal year that the asset is acquired or put into service and will be based on an estimate of the useful life of the asset.
  - Obligatory reserve funds will be maintained for growth, parkland and gas tax related capital projects. The growth related obligatory reserve funds will be fully funded from developer contributions. Components of the growth related projects which benefit the existing ratepayers or for which a discount has been given, shall be funded from tax/rate funding sources in the year the project is built. Notwithstanding, debt may be issued for growth projects when required in accordance with the *Development Charges Act, 1997, as amended*, and other pertinent City policies.

**i) Reduce Tax/Rate Supported Debt**

- i) As per the principles of the Council approved Capital Budget and Financing Policy, the City shall use reserve and reserve fund balances as a source of financing for capital projects.
- ii) When appropriate, the City shall use reserve and reserve fund balances as a source of debt substitution for capital projects which were previously approved with debt financing.
- iii) If discretionary reserves and reserve funds are below established targets, all or a portion of the future debt servicing cost savings resulting from reserve and reserve fund balances applied towards debt substitution shall be considered for future contributions to discretionary reserves or reserve funds at the discretion of the City Treasurer, it being noted that such contributions are subject to Council approval through the City's budgetary process.

**4.2. Reserve and Reserve Fund Management**

**a) Establishment and Modification of Reserves and Reserve Funds**

- i) Reserves and reserve funds shall only be established or modified if they are supported by a financial plan identifying the funding needs, targets, contribution sources, projected drawdowns and investment of funds.

- ii) Target funding levels shall be established for every reserve and reserve fund. Methods for calculating reserve and reserve fund targets shall be determined on a case-by-case basis considering the following:
  - Purpose of fund,
  - Certainty of end needs,
  - Best practices/standards regarding the identification of need and target balance levels (MFOA, GFOA, PSAB, etc.), and
  - Economic factors.
- iii) Reserve and reserve fund balances and associated targets shall be reviewed periodically to ensure adequate reserve and reserve fund levels are maintained for a ten year period.

**b) Investment of Reserves and Reserve Funds:**

- i) Reserves and reserve funds shall be invested for a term that will not exceed its expected date of need;
- ii) Reserves and reserve funds shall be invested in accordance with the Council approved Investment Policy;
- iii) Interest earned on reserves shall be recognized as revenue in the operating budget;
- iv) Interest earned on reserve funds shall be recognized as revenue in each specific reserve fund according to its proportionate share of the investment portfolio.

**c) Contributions To/Drawdowns From Reserves and Reserve Funds:**

- i) Contributions to/drawdowns from reserves and reserve funds shall be made in accordance with applicable resolution, by-law and this Policy.
- ii) Contributions to/drawdowns from reserves and reserve funds shall be approved by Council as part of the annual budget process, or specifically by resolution with the following exceptions:
  - Direct contribution to reserves and reserve funds such as development charges revenue;
  - Transfers that are a direct result of Council approved by-laws or resolutions such as Surplus/Deficit Policy;
  - Transfer of funds between reserves and reserve funds based upon adequacy analysis or other related information, at the discretion of the City Treasurer, or designate; and
  - Use of “revolving” reserves and reserve funds for the purpose approved by Council such as Workplace Safety Insurance Board claims.
- iii) Council approved contributions to/drawdowns from reserves and reserve funds not realized shall be reported to Council as part of the budget monitoring reports, or budgetary process.
- iv) Contributions to/drawdowns from reserves and reserve funds shall take into account intergenerational equity between current and future tax/rate payers.

**d) Lending/Temporary Borrowing of Reserves and Reserve Funds:**

- i) Intra-fund lending between reserves and reserve funds shall be permitted to temporarily finance capital and/or operating cash flow deficiencies to avoid external borrowing costs provided that all loans/transfers bear the City's internal rate of return and principal and interest are credited to the appropriate reserve or reserve fund source.
- ii) External loans shall be approved at the discretion of Council according to Section 107 of the *Municipal Act, 2001, as amended*, to any person, group, or body for any purpose considered to be in the best interest of the municipality. Prior to recommending such a loan to Council, staff shall consider the following:
  - External loans shall only be made to public agencies/groups and shall benefit the public;
  - The term of external loans shall not exceed five years;
  - Appropriate security shall be provided to protect the interests of the City;
  - A financial profile of the borrower;

- Are adequate reserves and reserve funds available for the term of the external loan; and
  - What rate shall the external loan bear and that principal and interest shall be credited to the appropriate reserve or reserve fund source.
- iii) All lending/temporary borrowing shall be provided from discretionary reserve and reserve fund balances as the loaning of obligatory reserve funds is prohibited under the *Development Charges Act, 1997, as amended*.
- iv) Under the *Development Charges Act, 1997, as amended*, debt may be included as a capital cost to leverage development charge (DC) revenue while waiting for DC collections to catch up to growth-related spending. Intra-fund borrowing between DC reserve funds is also permitted. In both cases, amounts borrowed must be repaid at the City's internal rate of return and principal and interest are credited to the appropriate reserve or reserve fund source.

**e) Termination of Reserves and Reserve Funds:**

- i) A discretionary reserve or reserve fund shall be terminated (wound down and closed) when the program or project it supports meets any of the following criteria:
- No longer in the scope of the City's strategic plans;
  - Program commitments have been completed and no future commitments are expected; and
  - The City Treasurer is confident that balances in other areas can mitigate the need to hold any remaining reserve or reserve fund balance.
- ii) Reserves or reserve funds identified for termination shall be reported to Council for review and approval. Reports to Council shall include recommendations regarding the timing of wind down, closure and the allocation of fund balances.

**4.3. Standard of Care**

**a) Delegation of Authority**

- i) Once Council approves reserves by resolution and reserve funds by by-law, the City Treasurer shall have overall authority for the reserves and reserve funds managed by the City.
- ii) The City Treasurer may delegate management authority over the reserves and reserve funds managed by the City to a designate.
- iii) The City Treasurer, or designate has the responsibility for setting reserve and reserve fund targets, it being noted targets will be periodically reported to Council through reserve and reserve fund reports (see Reporting Requirements below).
- iv) The City Treasurer, or designate shall have overall responsibility for this Policy, and the authority to implement a program for reserves and reserve funds and establish procedures consistent with the content of this Policy. Administrative responsibilities shall include, but are not limited to the following:
- Determines need for reserves and reserve funds for operating and capital budgets.
  - Sets targets for reserves and reserve funds in line with directives contained in this Policy and other pertinent policies.
  - As part of the reporting to Council, reviews and reports on the adequacy and continuing need for reserves and reserve funds managed by the City.
  - Preparation and presentation of reports and/or by-laws associated with the establishment, monitoring, or termination of reserves and reserve funds.
  - Develops appropriate practices, procedures and processes for the investment of reserves and reserve funds in line with legislative requirements, the City's Investment Policy and other pertinent policies.

- Prepares the City's long-term strategic financial plan with consideration of appropriate reserves and reserve funds to effectively meet the City's operating and capital budget financing needs.
- Ensures reserves and reserve funds managed by the City are in line with senior government statutes and agreements and other pertinent policies.

**b) Reporting Requirements:**

- i) The City Treasurer, or designate shall prepare the following reports regarding reserves and reserve funds managed by the City:
- Annual Audited Financial Statements - the annual audited financial statements shall include a statement of financial position, financial activities, and changes in fund balances for reserves and reserve funds.
  - Reserve and Reserve Fund Report - a financial plan forecasting reserve and reserve fund balances and a comparison to target objectives shall be prepared periodically based on the most current information available; this report may include the establishment of new, modification of existing and termination of existing reserves and reserve funds.
  - Budget Reports - reserve and reserve fund balances, projected contributions and planned drawdowns for a ten year period shall be presented in each multi-year budget. Annual changes to reserve and reserve fund balances shall be presented with each annual budget update, or specifically by resolution if required.
  - DC Reserve Funds Report - an annual report detailing pertinent information regarding DC reserve funds shall be presented to Council as required by the *Development Charges Act, 1997, as amended*.
  - Other reports in line with this Policy shall be brought forward to Council as needed.

**c) Policy Review**

- i) This Policy shall be presented to Council for review and update, if applicable, every four years, in the first year of each elected Council, or as deemed necessary by Council or the City Treasurer.