

## Upper Thames River Conservation Authority Board of Directors' Finance and Audit Committee Meeting Agenda

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Date: Friday May 24, 2024

Time: 9:30am

Location: 1424 Clarke Rd. London, Watershed Conservation Centre Boardroom

### **1. Modifications to the Agenda**

### **2. Declaration of Pecuniary Interest**

### **3. Administrative Business**

3.1. Minutes of the Previous Meeting: April 16, 2024

3.2. Business Arising from the Minutes

### **4. Budgeting and Reserve Plan – FA-05-24-04**

### **5. Adjournment**

Approved by Tracy Annett, General Manager

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**To: Finance & Audit Committee**  
**From: Christine Saracino, Supervisor of Accounting**  
**Date: May 24, 2024**  
**File Number: FA-05-24-04**  
**Agenda #: 4**  
**Subject: Budgeting and Reserves Plan**

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## **Recommendation**

The Finance and Audit committee receives this report for information and directs staff to develop a budgetary and reserve policy based on feedback received from the committee.

## **Background**

The UTRCA does not currently have a budget policy or a defined approach to long-term financial planning. A defined financial position is not yet linked to organizational goals. In the past we have primarily relied on annual efforts for program planning and have sought board guidance on setting levy increases without context of a broader set of financial plans for the organization including desired reserve balances.

Comprehensive corporate financial planning is required so that the organization can not only withstand unexpected impacts in its business environment, such as provincial or municipal change, economic change or environmental change, but also to ensure that resources are available for planned expenditures, both operating and capital project spending, beyond a single year.

In addition, as asset management planning is undertaken we need to ensure plans for capital spending have appropriate resources to action them.

## **The Task at Hand**

The Mandatory Programs and Services Regulation (O.Reg. 686/21) required our programs and services be separated in our 2024 budget. Through this process it became evident that mandatory programs and services have the greatest degree of underfunding. As an Authority, we are required to engage in this group of programs at the same time that the province has continued to reduce and freeze transfer payments and set a freeze on planning fees. It therefore appears the province is resting the cost of these regulatory programs on the Authority and its members to fund. Additional mandatory planning efforts already underway include; Watershed Strategy, Lands Strategy, and Capital Asset management plans. These efforts should align with multi-year budgeting and allow the UTRCA to focus financial sustainability efforts on this group of programs. We must address:

1. The need to bring Mandatory category 1 programs to a point of sustainability; and
2. Ensuring the operating and capital resources required for Mandatory category 1 programs are available for critical flood control infrastructure, continued delivery of our planning and regulations mandate, management of our lands and requirements under the Clean Water Act.

Our planning context includes two unavoidable facts: our 2024 budget evidences a projected operating deficit in these programs of \$1.2M; secondly that we have approximately \$3M of operating reserves.

With this in mind, there are two critical points to emphasize prior to formulating any steps. First, our budget is our best plan at a given point in time only and is subject to change if and when contract opportunities arise. Any new contract secured in any other category of program reduces Category 1 total costs because it allows some corporate costs to be directed to and absorbed by that contract. Secondly, actual results will vary from the plan. Given our history and practice in budgeting, there is at times, a significant difference between plans and actual results. Assuming that the budget accurately forecasts actual expenses, between 2 and 3 more years will pass before we completely deplete the category 1 operating reserves of the organization. This is not sustainable.

There are three ways only that any category of programs will balance (i.e. have no planned surplus or deficit at the end of the year); that being the addition of revenues or the reduction of costs, or both. These options are described below:

### **Increases to revenues**

Not only has the province failed to increase our annual transfer payment to keep up with inflation, but reduced it beyond half in the mid '90s and then again by half in 2019. The province froze our planning fees affecting revenues in 2023 and is limiting amounts under the Clean Water Act as well. The remaining primary source of funds for provincially mandated programs is member municipalities. In 2024 the general distribution levy constitutes 59% of the cost of category 1 expenditures.

The committee requested information on the rate contributions must rise. See the tables below for the two options considered for 2024.

**Option 1** - Increase general distribution levy by 29.8% to deliver a budget with approximately the same deficit as projected for 2023. With additional deliverables came additional costs in 2024. It was also determined that continuing support for Category 3 programs would be more cost effective than eliminating them as a result of the contribution they make to cover some corporate overhead.

2024 Budget	Member Rates	Cat 1 Levy	Cat 3 Support	Capital Cat 1 Levy	Totals
<b>Option 1</b>	General distribution	6,382,339	607,951	350,000	7,340,290
	Special benefitting	1,359,300	-	1,038,059	2,397,359
	Budgeted Costs	12,454,797	4,992,712	3,183,957	20,631,466
	Support % of costs	59.3%	12.1%	42.7%	47.2%
	Change in support	29.8%	14.7%	409%	45.4%
	<b>Deficit</b>	(1,208,209)	(406,494)	(453,148)	(2,067,851)

Note: Category 2 and Other Category 3 Campgrounds are not included in the table above as they do not require municipal support.

**Option 2** - Increase the general distribution levy by 50% for Category 1 costs to eliminate the projected deficit of \$1.2M in Category 1. In light of the fact that we often budget deficits and produce surpluses, it was felt that this was an extreme option best avoided. It did, however, indicate that significant increases to member levy is necessary and the rate of contribution to costs needs to approach 70% in order for Category 1, mandatory programs to be fully funded.

2024 Budget	Member Rates	Cat 1 Levy	Cat 3 Support	Capital Cat 1 Levy	Totals
<b>Option 2</b>	General distribution	7,590,548	607,951	350,000	8,548,499
	Special benefitting	1,359,300	-	1,038,059	2,397,359
	Budgeted Costs	12,454,797	4,992,712	1,038,059	20,631,466
	Support % of costs	71.9%	12.1%	42.7%	53.1%
	Change in support	50%	14.7%	409%	63.5%
	<b>Deficit</b>	0	(406,494)	(453,148)	(859,642)

Note: Category 2 and Other Category 3 Campgrounds are not included in the table above as they do not require municipal support.

It is known that CAs in the province, have a range of contribution of levy to costs for Category 1 programs ranged from approximately 30% to 90%. In 2024, ours is 59.3% for general levies, and 42.72% for capital directed levies.

Member levy is the largest contributor to Category 1 programs. Other levels of government combined only provide a fraction of what member municipalities do. Revenues from other levels of government limited, often capped, reduced and otherwise only available through governments' wish to fund programs. This varies year by year making it an unpredictable revenue source for mandatory programs. Only pressure on governments to increase transfer payments and offer more and greater levels of support for mandatory programs will enable the Authority to increase revenues from this source.

The next largest source of revenue for Category 1 programs is user fees. Currently, the Authority has a policy of capturing the cost of the planning and regulatory program to 50% through user fees, the limitations placed by the province which cap those fees make abiding by our own policy exceedingly difficult at the same time that demand for service is rising and response time for development applications is very clearly defined. Again, it appears the province is now requiring us to supplement the revenues lost to frozen fees from municipal levy.

Several other smaller sources of revenue to Category 1 programs have been developed over time. Revenues from land use agreements that fall into Category 1 have the potential to increase over time as leases renew, but they are market driven. Investment revenue is limited by the extent to which risk is deemed acceptable and the size of the investment pool. Donations, aside from recent donations of large land parcels, dwindle over time as inflation rises and economic circumstances put pressure on donors. We do not have a planned giving campaign in place; the rewards of which are debatable given the cost to administer and promote such a campaign.

That being said, steps need to be taken to supplement category 1 program revenues. There is little room for creativity here because in doing so, we must take care that we do not create a category 3 program intending that the revenues be attributed to category 1 costs. An example of such is the development of a tree nursery on Authority lands. The management of a tree farm is not provincially mandated and therefore not Category 1, so any profits by it would be attributed to Category 3 programs. Options are few. The very nature of Category 1 mandated programs prescribe that they must be primarily publically funded. However, we could,

1. Make a concerted effort to lobby the province for the regulatory planning fees freeze to be lifted.
2. Equally, convince the province that higher levels of Transfer payments for Category 1 activities are required. Set fees to cover a larger percentage of costs under the user pay philosophy. This could be full cost recovery fees which would help defray levy demands.
3. Review land management agreement rates to market values (underway)

4. Seek more profitable investment opportunities for greater investment revenue. This may include land sales and investing the sale proceeds.

### **Decreases to Costs**

The single largest cost in Category 1 programs is wages and their ensuing mandatory employment costs (79.6% of total costs). The single largest controlling factor of wages is our wage grid, which all employees fall under, not simply those whose work is related to Category 1 programs. We are a single organization and we are non-unionized. Multiple grids would raise costs. In 2022 a comprehensive evaluation by a consultant was conducted and whose recommendations were adopted the Board. It was estimated at that time that wages costs would rise approximately \$1.2M per year. The impact to levy in 2023 from the grid change was estimated to be 10.3% and in 2024 was 8.1%. Of the increase to levy in 2024, at least 8.1% is directly attributable to the change in the grid done in 2022.

The annual grid increase is a recommendation from staff to the board which is embedded in the budget presentation each year. All recommendations for change to the grid are made with consideration of market factors for hiring and retention, affordability, inflation and a peer comparison. The average annual wage in 2023 for 1 FTE was \$64,854 and we need to continue to undertake market comparisons in order to offer competitive wages to hire and retain staff.

Wages come with other mandatory employment related costs (MERCs) which in 2023 added 25% to wages on average across the Authority. This rate normally ranges between 25% and 28%. These additional costs include CPP, CPP Enhancement, Employment Insurance, Employer health tax, Workers compensation insurance, OMERS and a group benefits and health insurance program. Only the benefits contract cost is under our control. CPP rates have been rising for several years due to Service Canada's program to enhance CPP benefits. This will continue to be felt for a number of years. OMERS is now offered to all employees from the start of their employment. By and large, the 25%-28% MERCs will persist.

The second largest group of costs in Category 1 programs is depreciation expense (10% of total costs) which represents the cost of capital spending in all earlier years. This cost is now fixed. We currently have \$25M of undepreciated assets, of which \$9.9M falls in the flood control group. At the current rate of depreciation, our assets will be fully 'paid for' in 39 years on average, however each year, we add to this cost through capital spending decisions.

This leaves approximately 10% of costs in category 1 (or \$1.2M) which are controllable but also likely unavoidable. They are spread across the activities and programs conducted by Planning and Regulations, Water Management, Lands Management, Provincial Water Monitoring, Drinking Water Source Protection, Watershed Management and other corporate costs. Those costs include among others IT/network services and software subscriptions, contractor costs for lands maintenance, supplies,

signage, fencing where required, PPE, fleet costs, insurance, staff training and certifications, and CO levy.

The uncertainty in early 2020 due to COVID created the possibility that the parks would not open that year. This would have resulted in a significant impact to Authority finances given that the parks support 25% of corporate costs. We reviewed in detail all categories of costs and initiated cost saving measures. In the last 4 years we have already undertaken vendor review of banking fees, merchant services, telephone lines and internet services, as well as data back up and storage costs. We have spent considerable time reviewing property values for insurance purposes and are currently reviewing waste management costs and office stationery costs. In addition we have had two tax audits in the last 6 years to be certain we are correctly capturing all possible GST/HST rebates we are entitled too. For this reason we expect that additional cost saving efforts might yield approximately 5% cost savings, which does not include wages. This might net the organization approximately \$60K or 5% of our category 1 deficit in 2024.

We have alluded to the fact that non-category 1 programs help support costs corporate costs. This happens through an allocation system. We first ensure that all costs directly attributable to a program or program area are directed there. Of the remaining common costs, we allocate to programs based on the relative weighting of FTEs as a proxy measure of effort those programs require. In our 2024 budget, we have allocated \$1.488M of corporate costs in category 1 to other categories of programs so that every program bears some burden of the broader organization. It is important to recognize that this is decades old practice of the Authority and one which not all Authorities undertake. It too has resulted in reducing the impact on member levy and will continue to do so. It also speaks to the lack of reserves we have today.

### **A Combined Approach**

As we continue to review our budgets and planned expenditures for 2025 and beyond, we may make strides in cost reduction if we can find a grouping of costs where vendor negotiations seem fruitful. It is not expected that significant reductions in cost can occur without changes to compensation across the organization, and that would impact more than Category 1 programs. This is not deemed desirable in this labour market, at this time.

At the same time, we should carefully review all Category 1 capital spending needs. While this tactic does not speak specifically to the need for general distribution levy, it does dictate the special-benefitting levy amounts. The distinction between the two types of levy is perhaps not as well understood as it might be. Capital spending impacts today's need for special-benefitting levy and tomorrow's future costs. We must take care to ensure they are matched as best as possible within the constraints of needed capital repairs and member ability to pay.

There is strong argument that it should fall to government to support mandatory Category 1 programs. With the province pulling back support for many decades already, there is an uphill battle to be fought with the result unknown. Continued downloaded costs to municipalities may also be expected.

We need to have the freeze on fees lifted, and we will need to revise our policy on cost recovery to move it closer to the 100% mark in preparation of that.

We should take active steps to sell surplus land for investment purposes to assist in defraying Category 1 demand for levy as well. This needs to be undertaken sooner rather than later.

Finally, where costs exceed budgeted amounts, we need to define why and take steps to improve our forecasting ability.

### **Planning for Reserves**

Better planning, and by extension, budgeting, will help assist in predicting appropriate reserve balances. By and large, low levels of reserves do not become a serious matter until the time arrives when you need them. Ten years ago, it was perhaps not predictable that the province would change the CA Act to the degree it has, or that an increase to annual transfer payments would never be made.

These events, and others, necessitate that some degree of attention needs to be paid to reserves and their adequacy. Because we have flood control structures which need to be maintained for the safety of people and property, adequate reserves can only be determined with a carefully built set of project plans which incorporate the need for levy and current reserve balances. Equally discussions need to be held with the specific benefitting municipalities over those plans. We are approaching the point where this can happen.

In the meantime, we must push ourselves to predict what we believe will happen 3 or 5 years hence along with what we want to happen. Everyone has a role to play in that exercise.

### **Recommended by:**

Christine Saracino, Supervisor of Finance