



The Corporation of the Township of
North Huron

Reserve and Reserve Fund Policy

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SECTION A - POLICY OVERVIEW

1. Purpose

- 1.1 The policy establishes guiding principles, primary objectives, key management and administrative responsibilities, and standards of care for reserves and reserve funds managed by The Township of North Huron.
- 1.2 The purpose of this policy is to address some of the longer-term funding strategies for the Township and to ensure good financial and cash management for the ongoing financial stability of the Corporation. In conjunction with investment and debt management policies, this policy will inform decisions relating to long-range financial planning for capital projects in order to minimize both debt servicing costs and significant annual budget impacts by allocating costs to benefiting users over a number of years through the prudent use of reserves and reserve funds.
- 1.3 Reserves and reserve funds shall be established for the following purposes:
 - a) To facilitate long-term financial planning
 - b) To plan for asset management and the impact and financing of major capital projects
 - c) To provide for the cost of equipment or facility replacements
 - d) To smooth tax rate impacts and revenue fluctuations
 - e) To smooth expenditures which would otherwise cause fluctuations in the operating budget
 - f) To absorb the cost of one-time expenses not included in the operating budget
 - g) To fund future obligations

2. Scope

- 2.1 This Policy applies to all reserves and reserve funds administered by the Township, including those administered for any Local Boards, Commissions, Agencies, or Corporations.
- 2.2 Furthermore, the Policy applies to all Township employees who are responsible for the establishment, monitoring, administration and management of the Township's reserves and reserve funds.
- 2.3 All Reserve and Reserve funds will be managed in accordance with the Municipal Act.
 - a) Section 290 (4) (g): In preparing the budget for a year, the local municipality may provide for such reserves as the municipality considers necessary.
 - b) Section 293: specifies that the Minister may make regulations requiring a municipality to establish a reserve fund designated for prescribed liabilities, defining "liabilities", requiring a municipality to make payments into the reserve fund, prohibiting the municipality from changing the purpose for which the reserve fund is designated; and prescribing the conditions under which the municipality may change the designation of all or any part of the reserve fund, and borrow from the reserve fund.
 - c) Section 417: allows a municipality to provide in its budget for the establishment or maintenance of a reserve fund for any purpose for which it has authority to spend money and that a municipality may by bylaw provide that the money

raised for a reserve may be spent or applied to a purpose other than for which the fund was established

3. Review

3.1 The Reserve and Reserve Fund Policy will be reviewed every 5 years or earlier as needed.

4. Definitions

For the purpose of this policy:

- 4.1 “**Budget**” means an estimated financial plan of revenue and expenditure for a set period of time.
- 4.2 “**Capital Asset Renewal & Replacement**” means a category of reserve funds established to provide funding for the repair and maintenance of existing assets to ensure township-owned assets do not deteriorate over time.
- 4.3 “**Capital Asset Growth**” means a category of reserve funds established to provide funding to new capital initiatives while allowing the Township to stabilize the cost of purchasing major capital assets by spreading the cost over multiple years.
- 4.4 “**Contingencies/Stabilization & Risk Management**” means 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.
- 4.5 “**Debt**” means 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.
- 4.6 “**Development Charges Background Study**” means the background study undertaken by the Township for its current Development Charges By-law.
- 4.7 “**Discretionary Reserves and Reserve Funds**” means 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.
- 4.8 “**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.
- 4.9 “**Intergenerational Equity**” in economic, psychological, and sociological contexts, is the concept or idea of fairness or justice between generations.
- 4.10 “**Liquidity**” means a measure of an asset’s convertibility to cash.
- 4.11 “**MFOA**” refers to the 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.
- 4.12 “**Obligatory Reserve Funds**” means 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 Township. Obligatory

reserve funds are to be used solely for the purpose prescribed for them by statute or agreement.

- 4.13 **“PSAB”** refers to the Public Sector Accounting Board, an independent board with the authority to set accounting standards for the public sector.
- 4.14 **“Reserve”** means 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.
- 4.15 **“Reserve Fund”** means funds that have been set aside either by a by-law of the Township 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.
- 4.16 **“Revolving Reserves and Reserve Funds”** means 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.
- 4.17 **“Specific Projects & New Initiatives”** means 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 Township to save for planned or unanticipated projects or expenses that may arise and do not have another funding source.
- 4.18 **“Treasurer”** means the Township’s Treasurer/Director of Finance or Designate.
- 4.19 **“Township”** means The Corporation of the Township of North Huron.

5. Reporting

- 5.1 The Treasurer, or designate shall prepare the following reports regarding reserves and reserve funds managed by the Township:
- a) Annual Audited Financial Statements - the annual audited financial statements shall be prepared in accordance with Public Sector Accounting Standards.
 - b) 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.
 - c) 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.
 - d) 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.

SECTION B – PRINCIPLES AND OBJECTIVES

1. Guiding Principles for Reserves and Reserve Funds

1.1 Budget and Strategic Plan

Reserves and reserve funds shall form an integral component of the Township's budget and strategic financial plan.

1.2 Liquidity

Reserves and reserve funds shall be kept at an adequate level to ensure the Township has sufficient cash flow to meet its financial obligations; including but not limited to:

- a) Replace and rehabilitate capital infrastructure assets as required;
- b) Supply funds for new capital assets identified in the Township's long-term plans, or that arise from time-to-time;
- c) Fund long-term contingencies and potential liabilities; and
- d) Provide a buffer for significant unanticipated expenditures, or loss of revenues beyond the control of the Township.

1.3 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

1.4 Credit Rating and Cost of Borrowing

Reserve and reserve fund balances impact the Township'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 Township's credit rating awarded by Bond Rating Agencies.

1.5 Reserve and Reserve Fund Types

The type of reserves and reserve funds the Township shall maintain are as follows:

- a) **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 Township. Obligatory reserve funds are to be used solely for the purpose prescribed for them by statute or agreement.
- b) **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.

2. Primary Objectives for Reserves and Reserve Funds (in priority order)

2.1 Adherence to Statutory Requirements

- a) It shall be the Township's practice to establish and maintain segregated reserve funds that meet all statutory obligations.
- b) Reserves and reserve funds shall be managed in accordance with the *Municipal Act, 2001*, as amended.

- c) Reserves shall be established by Council by-law which governs the purpose, funding sources, and drawdowns of the fund.
- d) Reserve funds shall be established by Council by-law which governs the purpose, funding sources, drawdowns, and investment of the fund.

2.2 Promotion of Financial Stability and Flexibility

- a. It shall be the Township'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):
 - i. Obligatory,
 - ii. Capital Asset Renewal and Replacement,
 - iii. Capital Asset Growth,
 - iv. Special Projects and New Initiatives, and
 - v. Contingencies/Stabilization and Risk Management.
- b. The Township 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

2.3 Provision for Major Capital Expenditures

- a) It shall be the Township'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:
 - i. 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.
 - ii. 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 Township policies.

2.4 Reduce Tax/Rate Supported Debt

- a) As per the principles of the Council approved Capital Budget and Long Term Debt Management Policy, the Township shall use reserve and reserve fund balances as a source of financing for capital projects.

- b) When appropriate, the Township shall use reserve and reserve fund balances as a source of debt substitution for capital projects which were previously approved with debt financing.
- c) 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 Treasurer, it being noted that such contributions are subject to Council approval through the Township's budgetary process.

SECTION C – RESERVE AND RESERVE FUND MANAGEMENT

1. Establishment and Modification of Reserves and Reserve Fund

- 1.1 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.
- 1.2 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:
 - a) Purpose of fund,
 - b) Certainty of end needs,
 - c) Best practices/standards regarding the identification of need and target balance levels (MFOA, GFOA, PSAB, etc.), and
 - d) Economic factors
- 1.3 Reserve and reserve fund balances and associated targets shall be reviewed periodically to ensure adequate reserve and reserve fund levels are maintained.
- 1.4 Any change to the purpose for which the reserve or reserve fund is designated must be permitted by provincial statute and approved by by-law of Council. Before creating a new reserve or reserve fund, the option of adding an incremental contribution to an existing reserve or reserve fund of a like nature will be considered.
- 1.5 Reserves or reserve funds for different purposes shall be separate, but each may include a group of services in the same category. Flexibility can be achieved by defining, in the establishing by-law, the intended use in more general terms, such as "recreational purposes" rather than "swimming pool".

2. Investment of Reserves and Reserve Funds

- 2.1 Reserves and reserve funds shall be invested while ensuring adequate liquidity is maintained.

- 2.2 Reserves and reserve funds shall be invested in accordance with the Council approved Investment Policy.
- 2.3 Investment income earned on reserves shall be recognized as revenue in the operating budget.
- 2.4 Investment income earned on reserve funds shall be recognized as revenue in each specific reserve fund according to its proportionate share of the investment portfolio.

3. Contributions to/Drawdowns from Reserves and Reserve Funds

- 3.1 Contributions to/drawdowns from reserves and reserve funds shall be made in accordance with applicable resolution, by-law and this Policy.
- 3.2 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:
 - a) Direct contributions to/drawdowns from reserves and reserve funds such as development charges revenue, or Dearness Home gift donations;
 - b) Contributions to/drawdowns from that are a direct result of Council approved by-laws or resolutions such as Surplus/Deficit Policy;
 - c) Transfer of funds between reserves and reserve funds based upon adequacy analysis or other relate information, at the discretion of the Treasurer, or designate; and
 - d) Use of “revolving” reserves and reserve funds for the purpose approved by Council such as Workplace Safety Insurance Board claims.
- 3.3 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.
- 3.4 Contributions to/drawdowns from reserves and reserve funds shall take into account intergenerational equity between current and future tax/rate payers.

4. Target Levels for Reserves and Reserve Funds

- 4.1 Reserves and reserve funds are a critical component of the Township's long-term financing plan and offer liquidity which enhances the Corporation's flexibility in addressing operating requirements and in permitting the Corporation to fund capital projects internally. Municipal credit rating agencies recommend a debt to reserve ratio of \$1 in reserves for every \$1 in debt. By adherence to the Asset Management Plan, and subsequent prudent financial management, the Township of North Huron will take steps to:
 - a) Limit its reliance on debt for financing infrastructure and to ensure that the total debt burden of the Township (per Schedule 74 of the Financial Information Return) does not exceed the total of all reserves and reserve funds (per Schedule 60 of the Financial Information Return).

- b) Ensure that Contingencies/Stabilization & Risk Management reserves and reserve funds are at least 10% of operating revenue (per Line 9910 of the Financial Information Return).
- c) Target Capital Asset Renewal & Replacement reserve fund annual contributions to be based on a percentage of the value of the relevant assets (currently assets valued at historical cost):
 - i. 2-3% Buildings
 - ii. 1.5-4% Transportation and linear infrastructure (Roads, Storm water, Waste water and Water)
 - iii. 5-10% Vehicle and Equipment

5. Lending/Temporary Borrowing of Reserves and Reserve Funds

- 5.1 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 Township's internal rate of return and principal and interest are credited to the appropriate reserve or reserve fund source.
- 5.2 External loans are generally discouraged due to the administrative effort associated with managing those loans. However, should Council elect to approve a loan to an external party, the loan should be in accordance with Section 107 of the Municipal Act, 2001, as amended. Prior to approving such loans, the following principles should be considered:
 - a) External loans shall only be made to public agencies/groups and shall benefit the public;
 - b) The term of external loans should not exceed five years;
 - c) Appropriate security shall be provided to protect the interests of the Township;
 - d) The financial profile of the borrower shall be reviewed;
 - e) Adequate reserves and reserve funds should be available for the term of the external loan; and
 - f) An appropriate interest rate shall be applied, noting that principal and interest shall be credited to the appropriate reserve or reserve fund source.
- 5.3 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.
- 5.4 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 Township's internal rate of return and principal and interest are credited to the appropriate reserve or reserve fund source.

6. Termination of Reserves and Reserve Funds

- 6.1 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:
- a) No longer in the scope of the Township's strategic plans;
 - b) Program commitments have been completed and no future commitments are expected; and
 - c) The Treasurer is confident that balances in other areas can mitigate the need to hold any remaining reserve or reserve fund balance.
- 6.2 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

SECTION D – STANDARD OF CARE

1. Delegation of Authority

- 1.1 Once Council approves reserves by resolution and reserve funds by by-law, the Treasurer shall have overall authority for the reserves and reserve funds managed by the Township.
- 1.2 The Treasurer may delegate management authority over the reserves and reserve funds managed by the Township to a designate.
- 1.3 The 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).
- 1.4 The 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:
- a) Determines need for reserves and reserve funds for operating and capital budgets.
 - b) Sets targets for reserves and reserve funds in line with directives contained in this Policy and other pertinent policies.
 - c) As part of the reporting to Council, reviews and reports on the adequacy and continuing need for reserves and reserve funds managed by the Township.
 - d) Preparation and presentation of reports and/or by-laws associated with the establishment, monitoring, or termination of reserves and reserve funds.
 - e) Develops appropriate practices, procedures and processes for the investment of reserves and reserve funds in line with legislative requirements, the Township's Investment Policy and other pertinent policies.
 - f) Prepares the Township's long-term strategic financial plan with consideration of appropriate reserves and reserve funds to effectively meet the Township's operating and capital budget financing needs.

- g) Ensures reserves and reserve funds managed by the Township are in line with senior government statutes and agreements and other pertinent policies