Town of Whitby Policy

Policy Title:	Asset Retirement Obligation
Policy Number:	F 200
Reference:	Public Sector Accounting Board (PSAB) Handbook, section 3280, Council Resolution #217-22
Date Approved:	September 26, 2022
Date Revised:	N/A
Approval:	Council
Point of Contact:	Financial Services – Treasury Services

Policy Statement

An asset retirement obligation is a “legal obligation associated with the retirement of a tangible capital asset.” The Public Sector Accounting Board (PSAB) has instituted a new accounting standard “PS 3280”, requiring all municipal governments to comply. This policy serves to ensure that the Town of Whitby is in compliance with the accounting and reporting requirements.

Purpose

The purpose of this Policy is to provide guidance on the accounting treatment for asset retirement obligations (ARO) and to establish roles and responsibilities for the various departments at the Town.

Scope

This Policy applies to all departments, branches, boards and agencies falling within the reporting entity of the Town of Whitby, that possess asset retirement obligations, including, but not limited to:

a) Assets with legal title held by the Town of Whitby
b) Assets controlled by the Town of Whitby
c) Assets owned by the Town of Whitby that have not been capitalized or recorded as a tangible capital asset for financial statement purposes

This policy applies to all assets that have an obligation in relation to the retirement of a tangible capital asset. This includes assets in productive use and assets no longer in productive use. The costs related to asset retirement obligations are predictable and their obligations to retire are unavoidable. PS 3280 applies to all assets controlled by the Town that have a legal or contractual obligation, as well as legal obligations that have been created by a promissory estoppel, to be permanently removed or restored.

Asset retirement obligations **include** activities such as (but not limited to):
- Asbestos removal (e.g. building materials, roads, parking lots)
- Aggregate pits,
- Leaseholds,
- Removal of underground storage tanks (oil or gas),
- Retirement of landfills

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Asset retirement obligations **exclude** activities such as:
- Costs relating to routine replacement or life cycle maintenance of tangible capital assets
- Remediation of contaminated sites,
- Improper use of a tangible capital asset,
- Unexpected events such as an unexpected contamination.
- Costs arising from a plan to sell

Asset retirement obligations are different from contaminated site liabilities, which are covered in PS 3260. Per PS 3260, the liability for contaminated sites normally results from unexpected contamination exceeding the environmental standards. Asset retirement obligations are not necessarily associated with contamination; instead, they result from acquisition, construction, development or normal use of the asset.

Index

1. Definitions

1.1. **Accretion expense:** the increase in the carrying amount of a liability for asset retirement obligations due to the passage of time

1.2. **Asset retirement activities:** all activities related to an asset retirement obligation. Examples include: decommissioning a TCA, remediation of contamination created by normal use, post-retirement costs, and costs of other TCAs acquired to perform post-retirement activities

1.3. **Asset retirement obligation:** a legal obligation associated with the retirement of a tangible capital asset

1.4. **In-scope assets:** assets that the municipality controls, there is a legal or contractual obligation for retirement of the asset and the resulting obligation is significant on a quantitative or qualitative basis

1.5. **Not in productive use:** an asset that is not currently in use to produce or to perform regular activities of the Town of Whitby

1.6. **Productive use:** an asset that is currently in use to produce or to perform regular activates of the Town of Whitby

1.7. **Professional judgement:** used in assessing the appropriateness of the measurement technique and can be supplemented by experience, third party quotes, and independent experts

1.8. **Promissory estoppel:** a commitment to a promise that could be considered to be legally enforceable

2. Roles and Responsibilities

2.1. This standard implementation involves many departments and requires the involvement of multiple stakeholders across the Town. Specifically, Financial Services, Legal Services, Operational Departments, and Council all play important roles in this process:

2.2. **Financial Services** is responsible for the development of policies for accounting and reporting of asset retirement obligations in accordance with the Public Sector Accounting Board standard 3280. This includes:

2.2.1. Financial Statement reporting and disclosure requirements.

2.2.2. Monitoring the application of this policy.

2.2.3. Investigation and resolution of any issues pertaining to asset retirement obligations with the respective stakeholder.

2.2.4. Acting as the liaison between the External Auditors and the operational departments impacted by the Standard.

2.2.5. Continuous monitoring and assessment of the asset retirement obligations on an annual basis.

2.2.6. Financial Services to support Legal and Operational departments on the completeness of the identification of legislation and regulations that would impact asset retirement obligations on a go-forward basis.

2.3. **Legal** is responsible for the interpretation of any legal, contractual, or regulatory obligations and to provide clarification and confirmation on asset retirement obligations that may exist. This includes:

2.3.1. Reviewing contracts and agreements to determine if an asset retirement obligation exists.

2.3.2. Reviewing regulatory or legislative obligations and any changes pertaining to these.

2.3.3. Legal and Operational and Financial Services departments to work together on the completeness of the identification of legislation and regulations that would impact asset retirement obligations on a go-forward basis.

2.3.4. Providing clarification where required.

2.4. **Operational Departments** are responsible for communicating with Financial Services any asset retirement obligations that become known, or change, in a reporting period. This includes:

2.4.1. Advising Financial Services of any changes to pre-existing assets, new TCA acquisitions, asset conditions, legislations, regulations, or contractual obligations.

2.4.2. Operational Departments to work with Legal and Financial Services on the completeness of the identification of legislation and regulations that would impact asset retirement obligations on a go-forward basis.

2.4.3. Advise Financial Services of estimated costs to retire the asset, changes to previously estimated ARO costs, if professional judgement and expertise can be applied. Otherwise, defer to engage a consultant.

2.5. **Council** is responsible for reviewing and approving policy and reviewing any policy updates.

3. Legislative Framework

3.1. Public Sector Accounting Board Handbook Section 3280, asset retirement obligations, is effective for fiscal years beginning on or after April 1, 2022, making this applicable for Town of Whitby on January 1, 2023, with its first annual reporting requirement for December 31, 2023.

4. Recognition

4.1. According to PS 3280, a liability for an asset retirement obligation should be recognized when <u>all</u> of the criteria noted below are satisfied:

4.1.1. There is a legal obligation to incur retirement costs in relation to a tangible capital asset;

4.1.2. The past transaction or event given rise to the liability has occurred;

4.1.3. It is expected that future economic benefits will be given up; and

4.1.4. A reasonable estimate of the amount can be made.

4.2. At initial recognition, if the tangible capital asset is in productive use and not fully amortized, the Town will increase the carrying amount of the related tangible capital asset and recognize a corresponding liability.

4.3. If the related tangible capital asset is fully amortized, no longer in productive use, or was never recognized as an asset the treatment is as follows:

4.3.1. <u>Fully amortized TCA, still in productive use</u> – although it is fully amortized, the historical cost basis exists and the asset retirement cost is added to the assets existing cost and expensed over the revised estimated useful life of the asset.

4.3.2. <u>No longer in productive use</u> – the asset retirement cost is expensed immediately as there is no longer a period of future economic benefit associated with the asset retirement costs, and the asset retirement obligation liability is still recognized.

4.3.3. <u>Unrecognized assets (expensed at purchase)</u> –the asset retirement cost is expensed immediately as there is no cost basis for the asset retirement cost to be attached to.

5. Initial Measurement

5.1. For initial measurement, the estimate of a liability should only include costs that are directly attributable to asset retirement activities. Directly attributable costs include, but are not limited to: payroll and benefits, equipment and facilities, materials, professional fees, and overhead costs. These costs may be based on requirements established in agreements, contracts, or other legal obligations.

6. Subsequent Measurement

6.1. At each reporting period, the carrying amounts of the ARO liability must be reassessed to consider new information, the discount rate, and other assumptions used.

6.2. Financial Services will be responsible for assessing the discount rate applied at each reporting period to ensure it is reasonable. The discount rate applied to asset retirement obligations may be based on rates such as the Region of Durham borrowing rate, Canada bond yield rates, or other similar rates.

6.3. An average inflation rate will be applied to the asset retirement obligations. It is assumed that the average inflation rate will be based on the estimated timeframe to retire the asset.

6.4. At each reporting period, the Town will recognize any changes to the liability resulting from; time passing as an accretion expense, and any changes to the time frame or the original amount of the estimate.

6.5. Any revisions to the TCA's carrying amount are included and amortized using a straight-line method over the useful life of the asset.

6.6. The liability for an asset retirement obligation continues to be recognized until it is settled.

7. Transitional Provisions

7.1. There are three options for transitional provisions when implementing this standard.

7.1.1. Prospective

7.1.2. Retrospective

7.1.3. Modified Retrospective

7.2. Refer to Appendix 1 for more details on each provision.

7.3. When selecting the provision, the municipality should consider what information it is able to collect with regards to the discount rate and assumptions.

7.4. The Town of Whitby will disclose and present the transition provision within its Financial Statements in Fiscal 2023.

8. Presentation and Disclosure

8.1. The liability for asset retirement obligation will be disclosed in the Town's audited financial statements and note disclosures.

9. Professional Judgement

9.1. When measuring an asset retirement obligation liability, the best estimate of the cost to retire a tangible capital asset should be used. This estimate is based on the available information at the financial statement date. To determine the best estimate, professional judgement is required. Professional judgement can include internal expertise, external consultants, or third party quotes. Depending on the complexity of the retirement costs and the time frame, external consultants may be required.

9.2. It should be noted that uncertainty when predicting the timing and the amount of the asset retirement obligation does not eliminate the obligation. If uncertainty presents, external consultation may be required.

10. Integration with other processes

10.1. The requirements as defined within PS 3280, asset retirement obligation, will be integrated with the various processes already established at the Town. Specifically, asset retirement obligations will be tracked and recorded within the Town's Asset Management Database and will be included in departmental year-end checklists to ensure the financial statement reporting is accurate and complete.

11. Appendix

11.1. **Appendix 1** – Transitional Provision Summary – Determining which transitional provision to select.

	Prospective Application	Retrospective Application with Restatement	Modified Retrospective Application with Restatement
Impact on Comparative Figures	Not restated	Restated	Restated
Date Liability Measured	Measured as of the date the legal obligation was incurred	Measured as of the date the legal obligation was incurred	Measured as of the date the legal obligation was incurred
Date of Discount Rate and Assumptions Used	Discount rate and assumptions used are those as of the date the legal obligation was incurred	Discount rate and assumptions used are those as of the date the legal obligation was incurred	Discount rate and assumptions used are those as of the first date of the current period (i.e. April 1, 2021)
Impact on Opening Comparative Figures (April 1, 2020)	No impact	Recorded as an adjustment to opening accumulated surplus	Recorded as an adjustment to opening accumulated surplus
Impact on Opening April 1, 2021 Figures	Asset retirement liability and related asset retirement costs initially recognized	Rolled forward from restated comparative figures	Rolled forward from restated comparative figures

Source: BDO Canada LLP; Assurance and Accounting: Asset Retirement Obligation (ARO): A Practical Approach to Section PS 3280; July 2019

This Policy is hereby approved by Council Resolution #217-22 on this 26th day of September, 2022.