Multi year Capital plan – Remapping Exercise
Continuation

April 24, 2023

Town of Lincoln

What are we discussing today?

- Capital Budget:
  - Capital Budget Recap
  - Debt and the Debt Limit
  - Financial Implications of Reduced Debt
  - Council Direction
- Recommendations
- Next Steps

Capital Budgeting

- The 10 Year Capital Forecast serves as a roadmap for staff and Council when considering not only the spending of money to buy new, or maintain its existing capital assets, but also to plan for the projects' long term funding so that the money is available when needed

- The 10-Year Capital Forecast is a "living document" with revisions occurring annually. These revisions are generally the result of:
    - Infrastructure stimulus programs
    - Needs studies and analysis
    - Resource availability
    - Inflationary adjustments

- Lincoln has experienced significant growth and with it, investment in numerous capital projects – a few examples, primarily funded by development charge dollars:
    - Rotary Park
    - Jordan Village
    - Campden Fire Station
    - Prokich Park
    - Rittenhouse Road & Drake Avenue

Capital Budgeting

- The Town currently owns approximately three hundred million dollars in assets comprised of roads; bridges; buildings; parks; underground water, wastewater and storm water infrastructure; streetlights; and vehicles, etc.

- This investment needs to be protected through planning for the repair or replacement of these assets to properly maintain them; and equally as important is the planning for the funding for these projects.

- Typically projects are divided into two major categories, replacement and repair (R&R) and Growth Related/New Assets (GR)

Previous Council direction on debt, financial management and policy development

- April/May 2018 Staff presented a financial sustainability plan to Council which included the following which was approved as a roadmap

  Financial Policy Framework
  - Align Financial Policies/Procedures to Sustainability Principles
    - a. Operating & Capital Budget Policies
    - b. Reserves and Reserve Fund Policies
    - c. Debt and Capital Financing Policies
    - d. Delegated Authorities & Financial Accountabilities
    - e. Financial Policy Approval and Administrative Policies

- Since then we have been working to address all these approved directions as part of financial sustainability

Debt and Long-term financial flexibility

General principles already embedded in Town process:

- The capital financing program will be managed in a manner consistent with other long-term planning, financial, and management objectives.
- Prior to the issuance of any new capital financing, consideration will be given to its impact on future ratepayers in order to achieve an appropriate balance between capital financing and other forms of funding.
- To the extent practicable, replacement assets as well as regular or ongoing capital expenditures (for example, annual replacement of firefighter protective gear) will be recovered on a “pay as you go” basis through rates, tax levy, user fees, or reserves and reserve funds.
- It is recognized that reserves must be developed and maintained, as outlined in the Town’s Reserve and Reserve Fund Policy, for all capital assets owned by the Corporation to ensure long-term financial flexibility.

Capital Planning & Municipal Debt

- Municipalities can only incur long-term debt for capital projects. They may not incur long-term debt for operations.
- Debt is not a source of revenues; it is a financing tool.
- It enables the municipality to spread the capital cost over multiple years while the debt is repaid, rather than financing the project in a lump sum. Interest is paid on the debt as well.
- When the debt is paid for by the tax levy or water and wastewater rates, it means that the capital project that it is being financed will be paid for by current and future taxpayers or ratepayers.

Reasons for taking on debt

Municipalities may take on long-term debt to finance infrastructure and other capital assets.

Spreading out the cost of capital projects over their useful lives: Municipalities may not have enough resources to directly pay for a project in one year. Borrowing allows them to spread out the cost of the project over its useful life and allows infrastructure costs to be paid not just by today's taxpayer, but by future users as well.

Limited internal and external financing sources: Municipalities may have limited access to internal financing sources like reserves or reserve funds. External financing sources include government grants (federal and provincial), fundraising or donations, which generally offer a limited source of additional funding.

Low interest rates or escalating project costs: If interest rates are lower than the rate of inflation for certain construction projects, it may make sense to borrow for a project sooner, rather than pay a higher cost for the project later.

Considerations when taking out debt

Need or urgency: Municipalities may wish to consider the urgency of the proposed project. For example, if public health and safety is a concern, there may not be time to set needed funds aside in reserves. Borrowing can be an effective tool when there is an urgent need for financing.

- Interest rates (Are they increasing or decreasing? Is it a good time to lock in?)
- Inflation rates (Are they increasing or decreasing? Are they higher or lower than interest rates?)
- Urgency of the project (Are there health and safety considerations?)
- Council priorities (Is it a strategic priority of Council?)
- Financial sustainability (Are our contributions to capital able to provide for and maintain our infrastructure and services?)
- Financial flexibility (Can we react to an unexpected situation?)

What is the debt limit?

- The Annual Repayment Limit (ARL) is the maximum amount that a municipality can pay in principal and interest payments on long-term debt

- The ARL is calculated by the Ministry of Municipal Affairs based on the most recent FIR. Then, the municipal treasurer must update the calculation based on any additional approved debt or long-term commitments.

- The limit is 25% of Net Revenues. Some municipalities implement an “internal limit” that is lower than 25%. This is a decision that is made by weighing out the benefits and risks of taking out debt.

How is the debt limit calculated?

25% of “Net Revenues” or “Own Source Revenues”

MINUS

Debt costs and annual costs of long-term commitments

EQUALS

Annual Repayment Limit

How is the debt limit calculated?

- “Net Revenues” or “Own Source Revenues” includes items such as property taxes, water and wastewater rates, and user fees. It excludes items such as grants, development charges, and proceeds on disposal of property.

- Debt costs and annual costs of long-term commitments include principal and interest on all debt, including development charge debt, but excluding tile drain loans. It also includes long-term commitments to hospitals and universities.

- Development charge (DC) revenues are excluded from the calculation but DC debt costs are included. This is because there is risk due to uncertainty in timing and amount of DC collections.

What are Development Charges?

- Recover the capital costs associated with growth within the municipality
- Based on the premise that “growth should pay for growth”
- Calculated based on the DC background study, approved by by-law, and collected from developers
- DCs can be collected over a 10 to 20 year horizon; the timing of collection is not under the control of the municipality
- Some of the infrastructure for growth related projects needs to be constructed before the development occurs (such as watermains)
  - Therefore sometimes we go into debt, ahead of time, and use the DC dollars to pay for the debt interest and the infrastructure
  - As Council has inquired, sometimes there can be pre-payment of DC’s

Why are we relying more on Debt ?

Lincoln is in a growth trajectory and phase

- Significant capital investments based on needs, growth and priorities over the last 4 years
    - 2020 – $31 million
    - 2021 – $16 million
    - 2022 – $34 million
    - 2023 – $48 million

- Important to note, as per policy, capital levy goes up by the construction price index (CPI) – on average up until the last few years this has been 1.5% each.

- These costs and projects are funded primarily by reserves/development charges

Other factors increasing debt usage:

- Rising costs due to inflation
- Growth related projects, funded by development charges
- Increased interest rates have raised the cost of borrowing

2023 Capital Budget Recap

- The 2023 Capital Budget was approved for $48.0 million, which represents a significant investment in infrastructure

- Some of the most significant projects were the Lincoln Avenue Road Reconstruction for $10.5 million, the Prudhomme's Watermain for $8.2 million, shoreline protection at $6.03M and Durham Road at $3.43M

- The funding sources for these projects were:
  - $1.9 million development charges collected in reserves
  - $33.2 million (future costs from debt - funded by development charges, water rates and other revenue sources)
  - $8.3 million other current reserve funds
  - $3.3 million grants
  - $1.3 million capital levy

Capital Budget Recap

- Previous budget meeting/kick-off:
  - The Treasurer indicated that in order to complete the 2023 priority capital works, debt upon completion of these works, would reach approximately 15% of Net Revenues
  - This is based on current projections of costs and current interest rates
  - Furthermore, if no remapping was to occur, the Town's debt would continue to increase

***Council agreed that after the budget was approved, there would be a remapping exercise to look at the capital forecast and establish guidelines so that projects can be prioritized and scheduled over the 10-20 year horizon**

- Council direction at the April 12th Budget meeting
  - Defeated were two motions on debit limits, staff were asked to present revised project outlook and determine next steps

Recap: Recommendation / Considerations

What was presented was the following:

- Development charge debt not to exceed rolling 3-year average of revenues (past 3 years)
- User rate funded debt on a per annum basis not to exceed 75% of forecasted revenue
- User rates to be adjusted annually to meet debt forecast
- Total user rate and levy related debt not to exceed 10%
- Total value of all debt not to exceed 18% combined – ***the driver is DC funded debt***
- Reserve balances to be maintained within approved thresholds
- New debt each year shall not exceed available debt threshold in current or future years
- Annual report to be provided to council on debt projections, reserve balances and any variances on capital works.

What is the impact of maintaining the current limits and not separating out rate, levy and DC debt %?

If we maintained the existing approach and policy and didn't do anything:

Based on previously approved capital projects, Lincoln's debt once projects are completed will reach close to a cumulative 15% of Net Revenues.

Therefore, potential strategies identified by staff if Council wants no increases:

1. In 2023, delay the following projects:
   - Lincoln Avenue Road Reconstruction $10,500,000
     (Would need to determine impact of delay on grant funding of $1,755,000)
   - Durham Road Reconstruction $3,430,000

   ** This would smooth out the debt in the short-term but not in the long-term.*

2. Minimal to no debt taken out from 2024 to 2031

What is the impact of status quo and no change or update to policy ?

3. More of a pay-as-you-go approach
    - Priority projects that can’t be delayed would need to be funded by tax levy increases or rate increases
        - This will result in higher recommendations for water/wastewater rates and higher tax levy increases
    - Development charge projects would be delayed until sufficient amounts are collected (10+ years)
        - This would impact DC study and support from industry on increases to development charges, resulting in appeals to our new DC bylaw
    - As an example, if the 2023 budget proceeded without issuing debt for the non-growth related projects, combined water and wastewater bills for the average customer would have increased approximately 80% increase.

In 2024 the following major projects would need to be prioritized and evaluated for funding options:

- 201932 - Greenlane Phase 1 (King St to Konkle Creek)
- 202167 - King St Road Reconstruction (Vineland) with Region
- 202240 - Rittenhouse Reimagined - MFR Library Branch Expansion
- Fire Vehicles
- 3110325 - Road Rehabilitation Program
- Fleet Replacement & Expansion
- 202094 - Lakeshore Roads and Shoreline Protection Project
- 202498 - West Avenue Sewer Upgrade
- 3110315 - Bridges and Culverts Infrastructure Program
- 202187 - Jordan Lions Park Master Plan & Renewal

In 2025 the following major projects would need to be prioritized and evaluated for funding options:

- 201916 - Vineland Fire Station
- 202211 - Bartlett Reconstruction from King St to South Service Road
- 202094 - Lakeshore Roads and Shoreline Protection Project
- 202158 - Jordan Station Road Reconstruction & Watermain Replacement
- 202187 - Jordan Lions Park Master Plan & Renewal
- 202142 - Prudhommes Waterfront Park
- 202511 - BDSS Site Redevelopment
- 202213 - William St Neighbourhood Reconstruction
- 202501 - 4th Ave AT Connection from 19th St to Jordan Lions Park
- 3110325 - Road Rehabilitation Program

In 2026 the following major projects would need to be prioritized and evaluated for funding options:

- 202187 - Jordan Lions Park Master Plan & Renewal
- 202211 - Bartlett Reconstruction from King St to South Service Road
- 202164 - 19th St Watermain and Road Reconstruction 4th Ave to Red Maple Ave
- 202502 - Thirty Rd Reconstruction (King St to south Limit)
- 202094 - Lakeshore Roads and Shoreline Protection Project
- 202213 - William St Neighbourhood Reconstruction
- 202317 - Fletcher-Davey Road Reconstruction
- 202214 - Greenlane Phase 2 & 3 (Konkle Creek to Bartlett Rd)
- 3110325 - Road Rehabilitation Program
- 3110315 - Bridges and Culverts Infrastructure Program

Considerations when looking at remapping and funding projects

Long-term capital planning is complex and there are many factors to consider. Currently on staff workplan is:

- The asset management plan (phase 3, to include all infrastructure assets, must be completed by July 2024)
- Reserve balances to be maintained within approved thresholds
- Development charge background study (pending)
- Water and wastewater rate study to be updated after the DC background study (as per Watson and Associates presentation on January 25, 2023)
- Project start dates for developments shovel ready (2023 / 2024)
  - Prepayment negotiations
  - Front-end agreement negotiations

*These will impact the forecast, and updated growth estimates will impact the calculation of what the tax levy or rate increases would be without taking on new debt.

Recommendation(s)

Tonight, staff seek Council's direction on the following:

Two projects remain not tendered yet, but close, there is potential we can **delay** commencement of two 2023 capital projects until spring 2024:

1. Lincoln Avenue – $10.5M ($1.7M in grants from senior levels of gov't)
2. Durham Road – $3.43M

* *Decision considerations – interest relates, project costs*

How projects 2024 and beyond in the forecast, should be prioritized in order to update the capital plan?

- health & safety
- council priority
- grant opportunities
- growth funded ?
- Other ?

Recommendation(s) continued

Council consider striking an ad-hoc capital financing/debt review committee to work through this over the coming months.

- 4 members of council
- Senior staff (CLT)
- Goal to report back with:
  I. a recommendation on capital program prioritization themes
  II. a recommendation on debt limits
  III. a draft debt policy
  IV. Review of staff project lists and updated project prioritization

Further Reading

Tools for municipal budgeting and long-term financial planning
https://www.ontario.ca/document/tools-municipal-budgeting-and-long-term-financial-planning#

Questions?

Comments?

Clarity?