MUNICIPALITY OF SOUTH HURON

2001

Debt Management
Asset Management
Capital Planning

COW Meeting August 30,2021

Overview Municipal Debt

Legislative constraints on municipal debt

- Permitted for capital financing only
- Term of repayment must not exceed the lessor of (i) the expected useful life of the associated capital investment and (ii) 40 years
- Adherence to Annual Repayment Limit regulation sets limit at 25% of own source revenues

Overview of Municipal Debt

- Funding municipal infrastructure is an important municipal challenge

- Debt is NOT considered a revenue source

- Risks and benefits must be balanced

Benefits of using debt as a source of financing

Promoting inter-generational equity	• To spread out the cost of a capital project over its useful life thereby allowing costs to be paid not just by today's users, but future users as well
Funding urgent or high-priority capital works	• To fund urgently needed or high priority capital works projects for which municipalities have limited access to other financing sources such as reserves or grants
Cost Sharing	• To leverage opportunities from other levels of government with cost-sharing requirements
Saving on project costs	• If interest rates are relatively low and construction costs are increasing rapidly, using borrowing to start a project sooner might help a municipality avoid potential, higher costs in the future

Risks when using debt as a source of financing

Financial Flexibility	Debt can limit the financial flexibility of the municipality by impairing its ability to meet its financial obligations in the face of changing circumstances.
Implications on service delivery	Debt can compromise the financial sustainability of the municipality if the payment of debt service charges require the municipality to reduce service levels, to increase fiscal burden on the community or to neglect other financial obligations.
Community Impact	Debt can impose unreasonable costs on current and future members of the community as the municipality must pay for the financing costs of borrowed funds (interest charges).

Key Trends in municipal borrowing in Ontario

- Most Municipalities in Ontario have long-term debt outstanding
- About half issued new debt in 2014 - 2018
- In 2018 small municipalities committed 4-6% of their net revenues to debt servicing costs
  - South Huron = 10%

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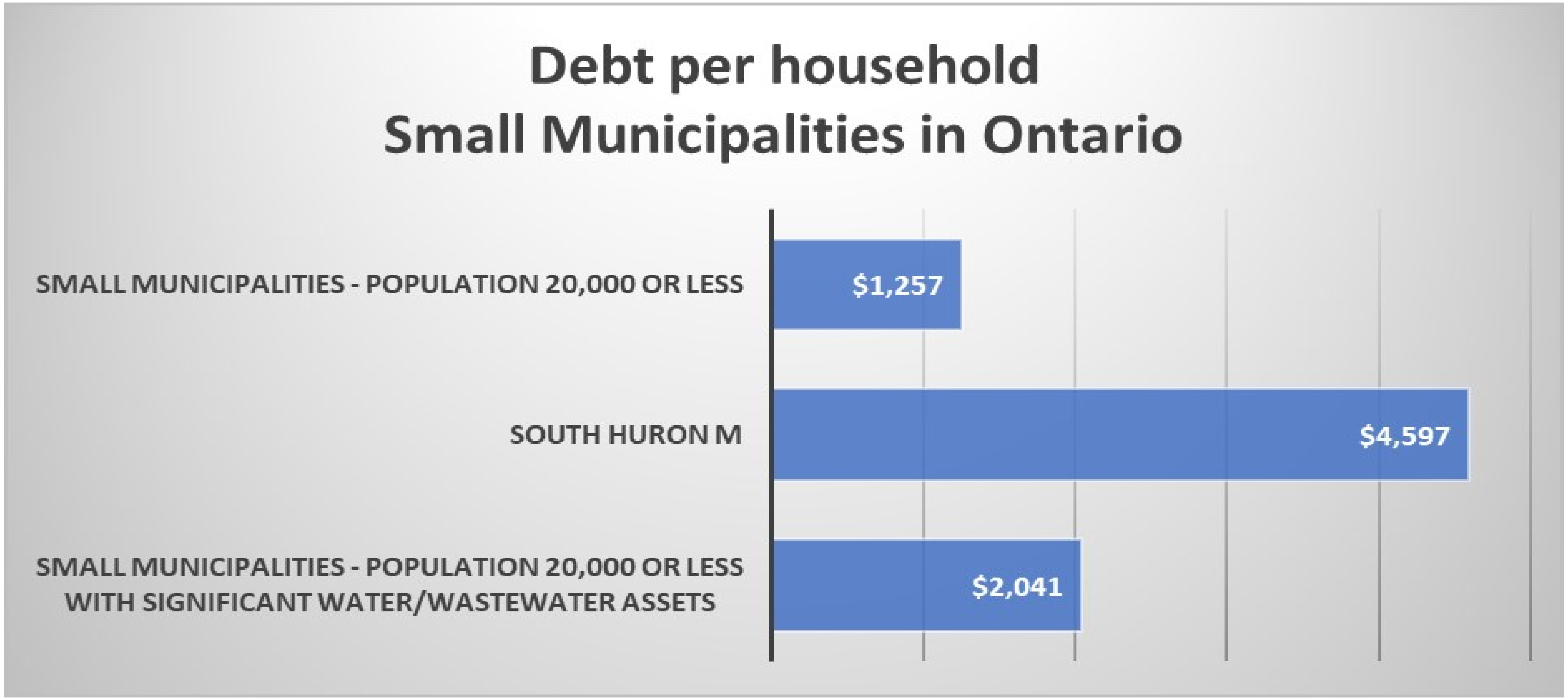
Data Source MFOA Municipal Debt Management webinar (FIR schedules)
Small Municipalities defined as less than 20,000 population

Key Trends in municipal borrowing in Ontario



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Debt Management Decisions

Debt Management decisions

Types of projects to be debt financed

- Capital projects only per legislation
- Rolling stock – will not use long-term debt

Sources of funding of debt servicing costs

- Tax Levy
- User Fees

Internal limits on debt issuance or debt servicing costs

- Internal limits
  - Debt servicing costs will not exceed XX% of own source revenues in order to maintain XX% flexibility to address emergency issues
  - Long term debt will not be issued where capital project is less than $XXX,XXX.XX

Debt issuance schedule

- Treasurer to ensure timing to match revenue sources…ie tax revenues received quarterly

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Debt Management decisions

Debt instruments utilized

- Construction financing
- Debentures
- Term Loans
- Leases

Debt structuring practices

- Maximum term
- Equal payments

Sources of financing

- Infrastructure Ontario debentures
- Canadian Bank term loans
- Reserves

Debt retirement strategy

- Once debt servicing costs are retired these funds to be used for capital

Debt Management policy decisions for South Huron

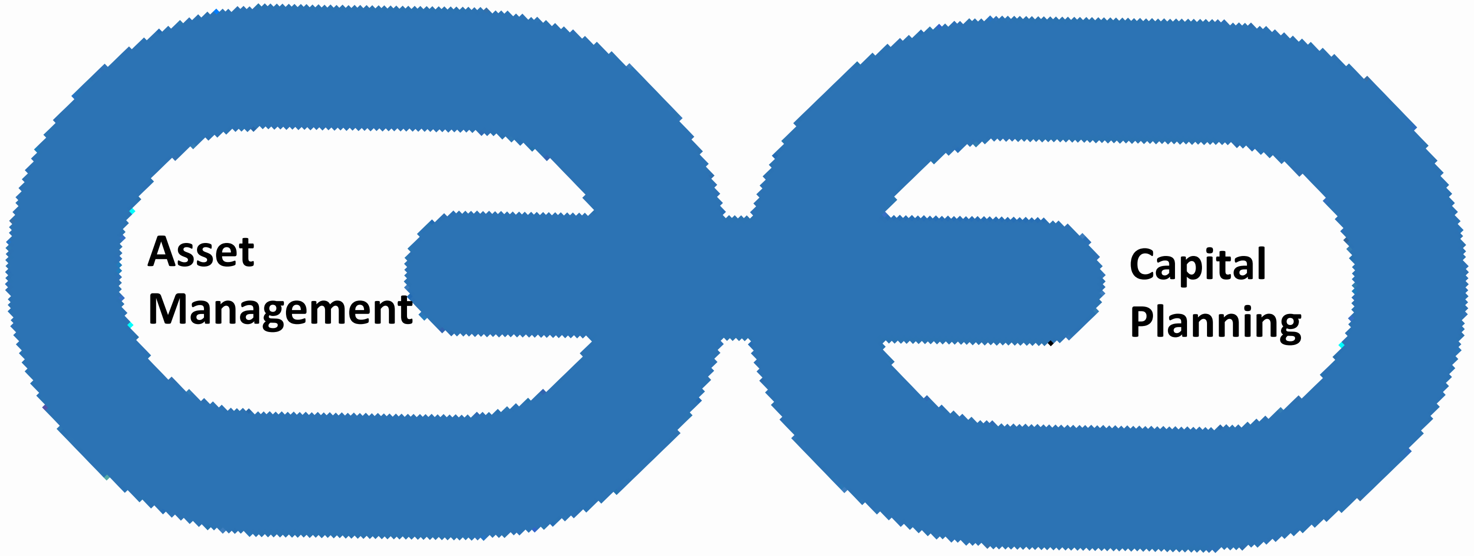
- Types of projects to be financed
  - ***Will <u>not</u> use long term debt to finance rolling stock and/or equipment as defined by policy***

- Internal Limits
  - Debt servicing limits
    - ***Debt servicing will not exceed XX% of own source revenues***
  - Debt Thresholds
    - ***Will not incur long term debt for capital projects valued less than $XXX,XXX.XX***

Debt Management policy decisions for South Huron

- Debt term restrictions
    - ***Term of debt will not exceed XX years***

- Debt Retirement Strategy
    - ***Retired debt servicing costs will be allocated to the infrastructure capital plan for the original funded source. This amount will not reduce the total base capital expenditure for that year.***


Asset Management
Capital Planning

Asset Management and Capital Planning

- **Asset management**
  - Systematic process of identifying current and future capital needs and developing strategies and projects to address those needs.
  - The projections in the plan are often as a result of information received from studies, master plans, state of infrastructure report and condition assessment reports.
  - Assists in prioritizing our infrastructure needs to mitigate risk and ensure established service levels are maintained.
  - Supports evidence-based business cases for capital planning

Asset Management and **Capital Planning**

- **Capital planning**
  - Capital plan is a financial tool
  - It is the process of budgeting resources for the future replacement and significant renewal/refurbishment of the municipality’s assets based on needs identified in the asset management plan.

Asset Management and Capital Planning

Asset Management Plan

Policies
- Debt Management
- Reserves
- Development Charges

Capital Planning

Capital Financing Strategy

Capital Plan

Levy/ User Fees

Gov't Transfers

Reserves and reserve funds

Development Charges

Debt

- ➢ Levy/User fees – 2021 AMP recommended annual increases for capital infrastructure deficit, plus increasing annual budget by applicable inflation
- ➢ Government Transfers – 2021 AMP recommended that the Canada Community-Building Fund (Gas Tax) and annual grants such as OCIF formula grant be allocated to Roads, Storm, Bridges/Culverts
- ➢ Reserves & Reserve Funds – maintain sufficient reserve to assist with capital sustainability
- ➢ Development Charges – Growth pays for Growth.
- ➢ Debt – follow debt management policy – what will be debt financed, terms, etc

Key finance strategy decisions for Council

- ***That South Huron increase tax revenues dedicated to capital expenditures (for infrastructure deficit) related to projects identified through the asset management plan. Options;***
    - ***Increase tax revenues by 2.5% per year for next 10 years***
    - ***Increase tax revenues by 1.8% per year for next 15 years***

- ***That the Canada Community-Building Fund (gas tax) and the Ontario Community Infrastructure Fund (OCIF formula based) grant revenues be allocated towards the road, storm and bridges/culverts asset categories***

Key finance strategy decisions for Council

- ***That South Huron increase existing and future infrastructure budgets by the applicable inflation index on an annual basis in addition to the deficit phase-in***

- ***That South Huron maintains sufficient reserves for future asset replacement by;***
- ***Options;***
  - ***Contribute 2% of the value of our capital assets per year to capital replacement reserve; or***
  - ***Contribute 1% of the value of our capital assets per year to capital replacement reserve***

Impact of AMP recommendations

Strategy to fund Infrastructure Deficit

Option 1 – increase tax revenues by 2.5% per year for next 10 years

Cost = $241,610

Tax rate increase of 2.8% Rural/1.97% Urban

Tax bill impact per $100,000 of residential assessment

= $16.25/year Rural

= $13.56/year Urban

Option 2 – increase tax revenues by 1.8% per year for next 15 years

Cost = $173,960

Tax rate increase of 2% Rural/1.4% Urban

Tax bill impact per $100,000 of residential assessment

= $11.97/year Rural

= $9.28/year Urban

Impact of AMP recommendations

Increase existing infrastructure budgets by applicable inflation index on an annual basis

CPI increase – projected at 3.1% (estimate based on June 2021 Stats Canada)

Cost = $299,800.

Tax rate increase of 3.5% Rural/2.5%

Tax bill impact per $100,000 of residential assessment

=$19.94/year Rural

=$17.25/year Urban

Impact of AMP recommendations

Contribution to Capital replacement reserves

Option 1 – contribute 2% of value of assets

Cost* = $4,635,350.

Tax rate increase of 51% Rural/42% Urban

Tax bill impact per $100,000 of Residential assessment

= $294.48/year Rural

= $291.78/year Urban

Option 2 – contribute 1% of value of assets

Cost *= $695,350

Tax rate increase of 7.8% Rural/6.2% Urban

Tax bill impact per $100,000 of Residential assessment

= $44.99/year Rural

= $42.29/year Urban

* Costs are calculated based on the percentage of the value of assets, less the current $3.2M contribution and less the ½% dedicated levy amount