

TIP SHEET 5: COUNCIL DECISION MAKING BASED ON THE EVIDENCE FROM THE ASSET MANAGEMENT PLAN

Introduction

This tip sheet will assist municipalities with asset management related decisions on issues such as funding, infrastructure deficit, setting priorities and expanding capital budgets when appropriate. Additionally, this tip sheet will explore the use of debt and some characteristics that municipalities can use to evaluate proposed infrastructure project requiring debt financing.

As asset management plans are presented to municipal councils, many jurisdictions are faced with decisions which can have different fiscal implications. Municipalities may be faced with decisions to implement increases to property tax or user fees to raise sufficient funds to carry out infrastructure related activities. The following questions may assist council in the decision-making process based on evidence from the asset management plan:

Should municipal council look at 100% cost recovery for property tax and user rate supported assets immediately?

Municipalities should be contributing to property tax and user fee supported reserves for the maintenance, repair and replacement of tangible capital assets, above in-year capital related expenditures.

Municipal asset management plans are often based on the estimated engineered design life of assets. Although this is a great tool and source of information to plan for future replacement activities, undertaking a complete replacement of an asset when the estimated life cycle is complete may be an ambitious goal in the short-term for a few reasons:

- Assets can remain in use past their estimated engineered design life; and
- Regular maintenance, repair and rehabilitation may extend the life of assets.

It is important that municipalities consider gradually progressing to a full cost recovery structure.

A general principal:

As a start, municipalities could target capital contributions of 1% per annum relative to the municipality's asset replacement value (of total asset base).

Example:

Asset replacement value of water and wastewater infrastructure = \$100 million

Annual Capital Contribution equal to 1% of \$100 million = \$1 million

Should municipalities consider establishing a formal policy on the level of reserve fund balance that should be maintained?

- It is essential that government maintain adequate levels of funds to offset current and future risks (i.e. revenues, shortfalls or unanticipated expenditures).
- Fund balances are a crucial consideration to long-term financial planning.
- Establishing a formal policy on reserves and reserve fund can assist a municipality to achieve short and long-term goals.
- The policy could identify:
 - the intended use of reserve funds;
 - the minimum and maximum reserve fund balances;
 - target balance; and
 - funding sources (e.g. dedicated revenues such as an infrastructure levy, development charges, funding for GO Transit, etc.).

Examples:

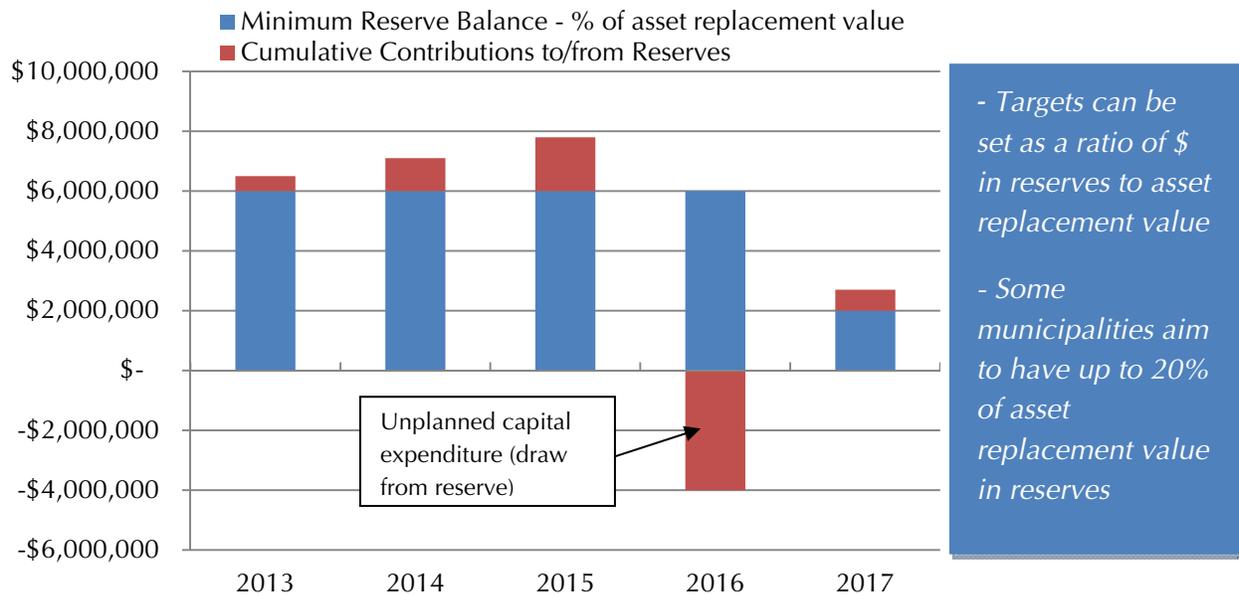
1. [County of Oxford](#)

2. [Region of York](#)

3. [Town of Halton Hills](#)

4. [City of North Bay](#)

Mitigating Unplanned Expenditures through Reserves



Maintaining a minimum reserve balance can help a municipality manage the costs of unplanned expenditures when they arise (as illustrated above). Maintaining a minimum reserve balance can mitigate increases to user rates or property taxes and could eliminate (or reduce) the municipality's use of debt to pay for capital works.

Shifting services from your property tax base to other user/rate supported areas (i.e. stormwater) can create funding room to support capital-related activities at a higher level. Municipalities may want to explore other unique revenue tools outside of the general tools outlined in Tip Sheet 3. The table below illustrates a few examples:

Revenue Tool	Description	Examples
Stormwater User Fees	<ul style="list-style-type: none"> - Transfers stormwater management funding from property tax base to a user-fee program - This funding model generally allows a municipality to dedicate funds to a typically underfunded area 	<ol style="list-style-type: none"> 1) City of Kitchener 2) City of Mississauga (January 2016) 3) Town of Richmond Hill
Parking Enforcement Enterprise	<ul style="list-style-type: none"> - Transform municipal parking division into a for-profit enterprise - Parking would become a user-pay system. - The cost of service is directed to those using the system - Removes parking costs away from property taxes 	<ol style="list-style-type: none"> 1) City of Kitchener
Non-Resident/Local User Fees	<ul style="list-style-type: none"> - Can be levied as a standard surcharge (\$ or %) to the resident rate - Can be applicable to individuals, families or groups 	<ol style="list-style-type: none"> 1) Town of Halton Hills 2) City of Pembroke 3) Town of Smith Falls

How your municipality could estimate the annual tax increase required to fully fund the asset base?

1. Identify the calculated annual provision (or capital contribution) to carry out repair, replacement and maintenance activities (See Tip Sheet 1);
2. Identify the difference in current capital funding vs. calculated capital contribution (Step 1 above);
3. Identify how much money is raised solely through property taxes; and
4. Divide the increase needed for capital spending (Step 2) by the amount of money raised through property taxes (Step 3). The result will be a percentage increase on your property taxes to fund the required annual capital contribution.

Example:

1. The 2014 calculated in-year capital contribution from your Asset Management Plan is estimated at \$4,000,000. This includes the required funds to carry out in-year capital related activities plus the funds contributed to an asset repair and replacement reserve.

2. In 2013, the municipality contributed \$1,000,000 to non-growth related capital activities. This includes money spent to carry out capital related activities plus the funds contributed to an asset repair and replacement reserve. This results in a difference of \$3,000,000.

3. In 2013, the municipality generated \$30,000,000 from property tax supported revenues.

4. In 2014, the municipality would have to raise property taxes by 10% to fund the additional \$3,000,000 capital expenditures. (\$3 million divided by \$30 million). It should be noted that this calculation assumes all other factors remain constant and the tax increase is only related to funding the additional capital requirements.

Many municipalities are finding it challenging to increase capital spending as operating costs, such as policing expenditures, hydro costs, and labour expenses, are growing. A few considerations:

1. Any small amount of dedicated funding for asset replacement can set a precedent for future increases;
2. There may be an opportunity to transition debt repayments when they retire to capital contributions as the "spending room" is already incorporated in the municipal budget; and
3. Municipalities that receive hydro dividends could dedicate a portion of this revenue to capital.

Is Having a Zero Debt Policy the Right Thing to Do?

Many municipalities have implemented policies to minimize or not consider the use of debt to carry out infrastructure related projects. A "no new debt policy" may be ideal theoretically, but carrying out such a policy may produce some negative effects for your municipality, such as:

- 1) Capital works are delayed, or not undertaken, or service levels are reduced;
 - a. Delaying the response to infrastructure needs in order to pursue a "no debt" policy can create an "infrastructure deficit" in a community (e.g. infrastructure is not maintained at required levels). This can reduce the service level that an asset can deliver. It may also increase the cost of replacement, repair, and maintenance over the long-term as the quality of the asset deteriorates.
 - b. This option can place a greater financial burden on future generations, as they incur costs to correct the "infrastructure deficit" created by earlier generations.

- 2) Borrowing up front may help leverage funds from other sources (Senior level government or private sector);

Municipalities can consider utilizing debt as a means to finance large infrastructure projects that provide benefits to a community over the long-term. Although the use of debt to carry out infrastructure related activities is a practical tool, the debt must be affordable and sustainable. The use of debt should only be taken on when the source of repayment is identified and are shown to be manageable.

When financing infrastructure, it is important that a municipality and Council answer the following questions:

1. Is the debt within your municipality's sustainability limits?
 - Within legislated limits? [Annual Repayment Limit](#)
 - Does your municipality have a debt policy?
 - Below are some sample examples of debt policies and debt management practices utilized by various municipalities
 - a) [City of Peterborough](#)
 - b) [Municipality of Meaford](#)
 - c) [Region of Peel](#)
 - d) [City of Airdrie, Alberta](#)
2. Have we ensured the debt is used for the right infrastructure projects?
 - Does the project provide long-term community benefits?
 - Debt is only used for infrastructure purposes (not for ongoing operating expenses).
 - Debt is not being used to carry out routine capital asset repair and replacement activities (e.g. annual capital road maintenance allocation)?
 - Is the term of the debt reflective of the useful life of the asset?
3. Is the debt structured with sources of repayment in place?
 - Increase in user fees or property taxes to support payments are quantified.
 - Will the debt affect other municipal services – reduced service in other areas?