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## **2020 Preliminary Draft Capital Budget Staff Report to Council**

Report Number: Assign Report Number in eSCRIBE.

Department(s): Financial Services

Author(s): Mike Mayes, Director, Financial Services/Treasurer

Meeting Date: October 28, 2019

### **Recommendations**

1. That the report entitled 2020 Preliminary Draft Capital Budget dated October 28, 2019 be received; and
2. That subject to any additional direction from Committee, that the proposed budgets be incorporated into the Draft Budgets to be presented to Committee of the Whole on November 25, 2019.

### **Executive Summary**

The proposed 2020 Capital Budget achieves the following:

1. Provides an achievable capital program
2. Does not increase the tax-supported Asset Replacement Fund (ARF) deficit
3. Applies 2020 increases in ARF contributions to the fund balance and not to capital projects
4. Conserves the additional Gas Tax payments received in 2019 for strategic purposes
5. Creates no new debt

## Purpose

This report provides details for the previous report, *2020 Budget Process Update*, dated October 15, 2019. It elaborates on the identified challenge. The preliminary draft budgets are the starting point for Council deliberation and will form the basis for the consolidated draft budgets to be presented to Committee of the Whole on November 25, 2019.

The specific challenges to be addressed are:

1. Developing an achievable capital program – the elimination of capital carryovers
2. Building capital reserve funds

## Background

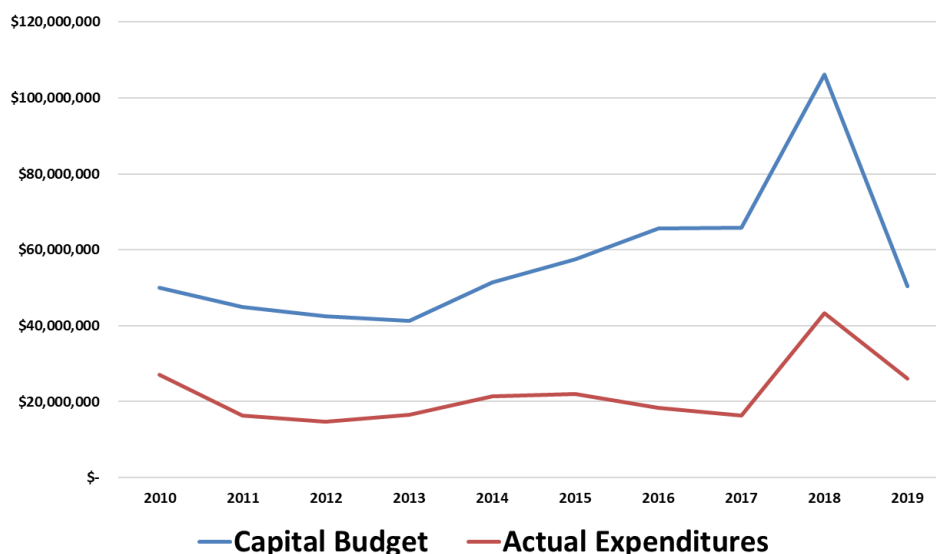
### The Capital Budget has significant challenges

1. Capital carryovers
2. Tax-supported ARF deficit

### Capital carryovers result when expenditures are below budget

Capital projects that are approved by Council and have funding applied to them, but are not completed by the end of the year, are Capital Carryovers.

Capital carryovers result when capital expenditures are below budget. Sometimes projects are completed for less than the approved budget, but the majority of the variances are from expenditures that have not occurred yet – capital carryovers.



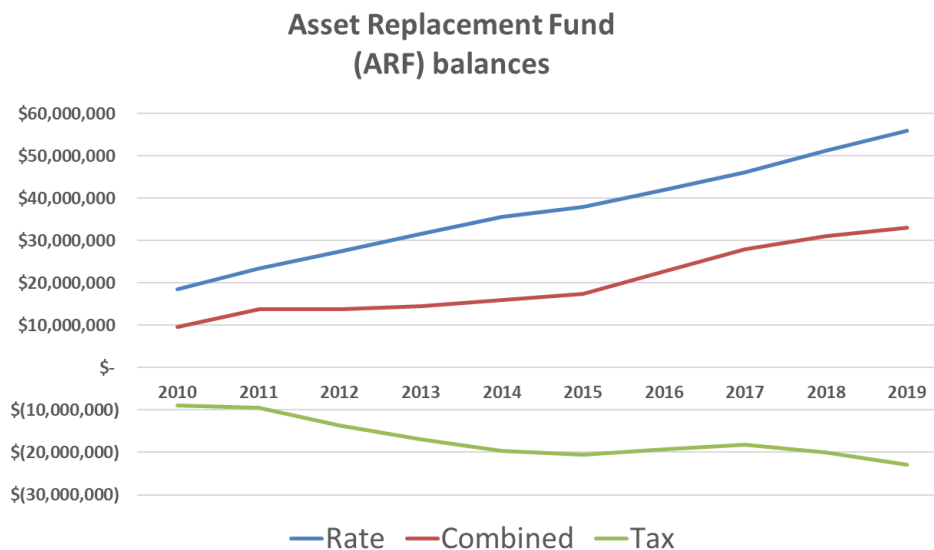
Capital carryovers create a number of issues:

1. Cash flow planning for investments in the middle to long-term is difficult because it is not clear when the cash will be required for projects. As a result, investments tend to be of a shorter term and more liquid to allow for flexibility.
2. Project delivery expectations are not being fully met. Completing less than half of the annual program has been the Town's experience.
3. The cost estimates, on which the budget is approved, can be out of date for a project that has been carried over for a couple of years.

In addition, capital carryovers look bad and give the impression that there may be inefficiencies.

### The tax-supported ARF is in a deficit

Although the overall Asset Replacement Fund (ARF) is projected to be \$33 million at the end of 2019. This is based on the strength of the rate-supported ARF (\$56 million); the tax-supported ARF will have a \$23 million deficit.



### Restrictions were applied to the 2020 capital budget

To deal with these challenges on an interim basis, new rules were applied to the creation of the capital budget:

1. The capital program is to be achievable. To eliminate capital carryovers, the “tender-ready” concept was introduced.

2. There is to be no increase in the tax-supported ARF deficit. As the \$23 million deficit is the net of all tax-supported ARF funds (roads, parks, facilities, library and fire, etc.), no draws on tax-supported ARF funds were allowed.
3. Any increases in ARF contributions are to be applied to the fund and not used to fund capital projects. The fund will never grow if it is just used as a flow through.
4. Conserve the additional Gas Tax payments received in 2019 for strategic purposes. In 2019 the Town will have received an additional \$2,594,820 (\$2,547,376 as a top up and \$47,444 as our share of the surplus). As these are one-time payments, they were not included in the initial funding for 2020.
5. There is to be no new debt. Although interest rates are extremely low, there are no unique projects that would make this a viable option.

In this year of policy transition, using options 4 (extra Gas Tax) and 5 (debt) are tempting. However, consideration must be given to the capacity to deliver and the priority of projects – application to the Mulock Farm in a future budget may be more appropriate.

## **Discussion**

### **A new financial strategy will be presented to Council in 2020**

The restrictions applied to the 2020 capital budget are just an interim step; the longer term solution is the creation of a comprehensive overhaul of our financial policies and strategies. An overarching fiscal framework, comparable to that of York Region, is targeted to be presented to Council in May/June of 2020.

It will include:

- New Financial Policies
  - ARF (Asset Replacement Fund) Strategy
- Revision of existing Financial Policies
  - A Budget Policy to formalize our current practices
  - A change in the Economic Increase Policy to an earlier target date to facilitate the preparation of budgets
  - Updates to the Investment Policy with regards to capitalizing on the long term opportunities that should materialize and the allocation of incremental Reserve Fund investment income
- Multi-year budgets
  - Capital plan linked to Asset management Plans and DC Background Study
  - Operating budget outlooks
  - Update of the rate-supported financial plans

The results of the REV It Up service review may inform this process.

## **Projection shows \$60 million in capital carryovers from 2019**

2019 started with \$58 million in capital carryovers from 2018 and added another \$28 million in new budget approvals. Of the \$86 million in Council-approved budgets, it is estimated that \$26 million will be completed.

This will result in an estimated \$60 million in capital carryovers.

## **A capacity review re-sorted and re-prioritized capital requests**

In addition to the \$60 million in capital carryovers, there have been another \$30.5 million of new requests for 2020. These projects were diligently reviewed to determine if we had the capacity for them – the operational capacity to deliver them, and the financial capacity to fund them.

Each project was then sorted into one of the following categories.

Cancelled - \$4.3 million of projects were eliminated. These are projects that are no longer supported by the sponsoring department. They might be redundant or no longer required.

Deferred - \$35.7 million of projects have been deferred. These are projects that are supported by the sponsoring department but we do not currently have the capacity to deliver them. This could be because of priority (operational capacity) or funding (financial capacity). In this category are projects that are not tender ready. Projects in this category that had been previously granted funding by Council (carryovers) are to have their funding removed. These projects must be re-submitted for approval to go forward. This may occur in future years or on the budget year if capacity becomes available.

Capital Spending Authority (CSA) - \$50.5 million of projects are requesting capital spending authority. There is both the operational and financial capacity to deliver these projects. They are in process, tender ready, or are the cost to get tender ready.

The Capital Spending Authority is the total of all capital expenditures approved by Council and may span more than one year. This differs from the Capital Budget which is the annual component and includes approval of the required funding. The Capital Program is the list of projects to be delivered by the Capital Budget.

The requested CSA of \$50.5 million includes a \$39.5 million budget for 2020 and an \$11 million budget for 2021. The 2021 commitment is for the 2<sup>nd</sup> phase of projects that span two years - \$6.2 million for the new fire station and \$4.8 million for the smart meter project.

The following table provides an overview of how the capital budget has been re-sorted and re-prioritized

	New Requests	Carry-overs	Total
In \$ millions			
Category total	30.5	60.0	90.5
Cancelled	- 0.3	- 3.6	- 3.9
Deferred	- 21.2	- 14.9	- 36.1
<b>Capital Spending Authority</b>	<b>9.0</b>	<b>41.5</b>	<b>50.5</b>
2020	8.2	31.3	39.5
2021	0.8	10.2	11.0

### There are major projects in the Capital Spending Authority

To test the reasonability of operational capacity, major projects – those that have a high cost to effort ratio – should be identified. There are \$16.7 million in the 2020 budget. These items do not significantly distract staff in Engineering, Public Works and Procurement from delivering on the rest of the capital program.

	2020	2021	Total
In \$ millions			
Fire station 4-5	6.2	6.2	12.4
Other fire capital	4.4		4.4
Water meters	4.8	4.8	9.6
Parks development	1.3		1.3
	<b>16.7</b>	<b>11.0</b>	<b>27.7</b>
Other projects	22.8		22.8
<b>Total</b>	<b>39.5</b>	<b>11.0</b>	<b>50.5</b>

Fire Station 4-5 has a previously approved budget of \$11 million. The Joint Council Committee has conditionally requested a 15% increase. The opening is scheduled for 2021 and the costs have been spread over the two years. This project is managed by Town of Aurora staff.

Other fire capital includes 3 fire vehicles (\$2.7 million) and other items which are mostly managed by CYFS staff.

Water meters is the introduction of advanced metering infrastructure, a.k.a - smart meters. \$10 million has been previously approved for this project. Installations are to start in 2020 and the majority should be completed by the end of 2021. Staff have been seconded and contracted for this project.

Park development covers payments to developers for two parks – Glenway and Sundial.

That leaves all of the other projects, a total of \$22.8 million.

### **\$22.8 million for other projects should be achievable**

Excluding the purchase of the Mulock Farm in 2018, the Town spends approximately \$20 million in capital expenditures annually. 2019 is expected to reach \$26 million. On that basis, we should have the operational capacity to deliver the capital program.

### **There is adequate funding for the 2020 capital budget**

The following tables summarized the required sources of funding for the 2020 capital budget. This includes both new requests and previously approved budgets (carryovers).

	New requests	Carryovers	Total
	In \$ millions		
Asset Replacement Funds:			
Tax-supported	2.22	5.60	7.82
Water/wastewater	2.10	1.10	3.20
Stormwater	0.50	0.40	0.90
DC's	1.70	12.99	14.69
General	0.29	0.16	0.45
Reserves	0.00	1.12	1.12
Gas Tax	1.30	5.16	6.46
Other	0.04	4.82	4.86
<b>Total</b>	<b>8.15</b>	<b>31.35</b>	<b>39.50</b>

The capital budget restrictions were adhered to with one minor exception. CYFS will be drawing on its Asset Replacement Fund. This has been provided for in its Asset Management Plan and its 10-year operating budget forecast. In addition, it will be making transfers of its operating surpluses to its ARF. This has been approved by JCC (the Joint Council Committee).

To supplement its ARF, Stormwater will be drawing on the Stormwater Management Pond Maintenance reserve to fund appropriate projects.

Not all Growth capital is covered by DC's (Development Charges). Some service categories are subject to a mandatory 10% discount and need an additional source of funding. The 2020 request includes a project that is not eligible for DC funding. The total requirement of \$190,000 will be covered by growth reserve fund.

### **Procedural changes are being introduced for 2020**

A new approach to capital budgeting is being introduced.

Capacity reviews will be performed to ensure that we have both the operational and financial ability to deliver on our capital program. This will ensure the credibility of the program.

The "tender ready" approach means that projects will only be included in the budget if they are:

- Tender ready – all set to go, just waiting for budget approval
- Getting tender ready – the costs, if any, such as design that are required to get a project tender ready. The resulting project will still need to be submitted for separate approval when it is tender ready
- Active projects that have been previously approved

Regular reporting will be expanded. This will track the progress of the projects in the annual program. It will adjust the program for projects if it is determined that they will not be active or completed in the current year. In that scenario a request will be made to modify/cancel the project or defer it to the next year. If this opens up capacity, or if capacity already exists, there could be requests to add deferred projects to the program. However, these adjustments must remain within the approved annual budget. This process will be tested over the year.

## **Conclusion**

The 2020 capital budget includes some significant procedural changes. In conjunction with that, we are commencing a comprehensive overhaul of our financial policies and strategies. An overarching fiscal framework, comparable to that of York Region, is targeted to be presented to Council in May/June of 2020.

### **Upcoming dates:**

- November 11 – Special Committee of the Whole – Tax-supported Operating Budget
- November 25 – Committee of the Whole regular meeting with draft budgets and fees and charges for approval



- December 2 – Target for Council approval of the Budget

There will also be opportunities for Councilors to meet with or to obtain additional information from the Treasurer or other members of staff.

## **Business Plan and Strategic Plan Linkages**

This report links to Council's strategic priority of long-term financial sustainability by developing a multi-year operating and capital budget that aligns with the Budget Policies.

## **Consultation**

Members of the Senior and Operational Leadership Teams participated in the preparation of the budget.

The Library Board approved the Newmarket Public Library budget request on September 18, 2019.

The Joint Council Committee (JCC) approved the Central York Fire Services (CYFS) request on October 24, 2019.

## **Human Resource Considerations**

The capital budget requests do not directly impact staffing levels.

## **Budget Impact**

The Capital Spending Authority includes \$50.5 million in expenditures - \$39.5 million for the 2020 budget and \$11 million for 2021.

The new budget has projects that will generate ongoing operational costs or savings.

In the Tax-supported operating budget

- \$1,012 of additional base costs for the Implementation of Administrative Monetary Penalty System for Parking Offences
- \$12,150 of additional growth costs for Active Transportation Implementation

In the Rate-supported Operating budget

- \$15,000 of savings in water expenses from the Fire Hydrant Barrel Cutter

## **Attachments**

Appendix A – 2020 Capital Budget Summary

Appendix B - 2020 Capital Budget Details

Appendix C – Capital Deferred Projects Summary

Appendix D – Capital Deferred Projects – Details

Appendix E – Cancelled Projects

## **Approval**

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Esther Armchuk, LL.B  
Commissioner, Corporate Services

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