Subject: 2019 Capital Budget

Report to: Budget Review Committee

Report date: ~~Thursday, January 10, 2019~~ **Thursday, February 14, 2019**

Recommendations

1. That the 2019 Capital Budget for the Niagara Regional Departments and Agencies, Boards and Commissions of ~~$273,939,966~~ **$274,283,966** as per **Appendix 1** to Report CSD 1-2019, **BE APPROVED IN PRINCIPLE** pending final by-law approval anticipated to be on February 28, 2019 and subject to approval of the Niagara Regional Transit separate levy being considered with the 2019 operating budget;

2. That financing in the amount of ~~$248,911,706~~ **$249,255,706** gross and ~~$227,101,255~~ **$227,445,255** net **BE INITIATED** upon approval of the 2019 Capital Budget and **BE ALLOCATED** to the projects as summarized in **Appendix 2** to Report CSD 1-2019; and

3. That the necessary by-laws **BE PREPARED** and **PRESENTED** to Council for consideration to coincide with the approval of the operating budget.

Key Facts

- The 2019 capital budget totals ~~$273.94~~ **$274.28** million and includes ~~168~~ **167** projects of which 161 with an estimated cost of ~~$248.91~~ **$249.25** million are supported by a full capital data sheet and are proposed to be initiated concurrently with the approval of the 2019 Capital Budget (Appendix 2). Six capital projects totalling $25.03[1] million will be brought forward for initiation at a later date once further information is available (Appendix 3). Budget detail including data sheets can be accessed through the eScribe meeting site under 2019 Budget Detail.
- The proposed 2019 Capital Budget can not be funded within 2% guidance as a result of significant one-time projects. A separate levy of 2.3% will be requested to support Niagara Regional Transit (NRT) operating and capital costs, of which 0.4% ($1.388 million) is to support the debt charges for NRT capital.
- In 2020, the Capital Budget will require an additional separate levy to support Long Term Care Redevelopment. The total 2019 Capital Budget and 9-year capital forecast is currently estimated to be $2.7 billion (Appendix 4).
- Should the operating budget deliberation not approve the amounts in excess of guidance; a deferral or reduction of $13.9 million or 5.1% of the 2019 gross levy capital program to be within 2% guidance will be required.

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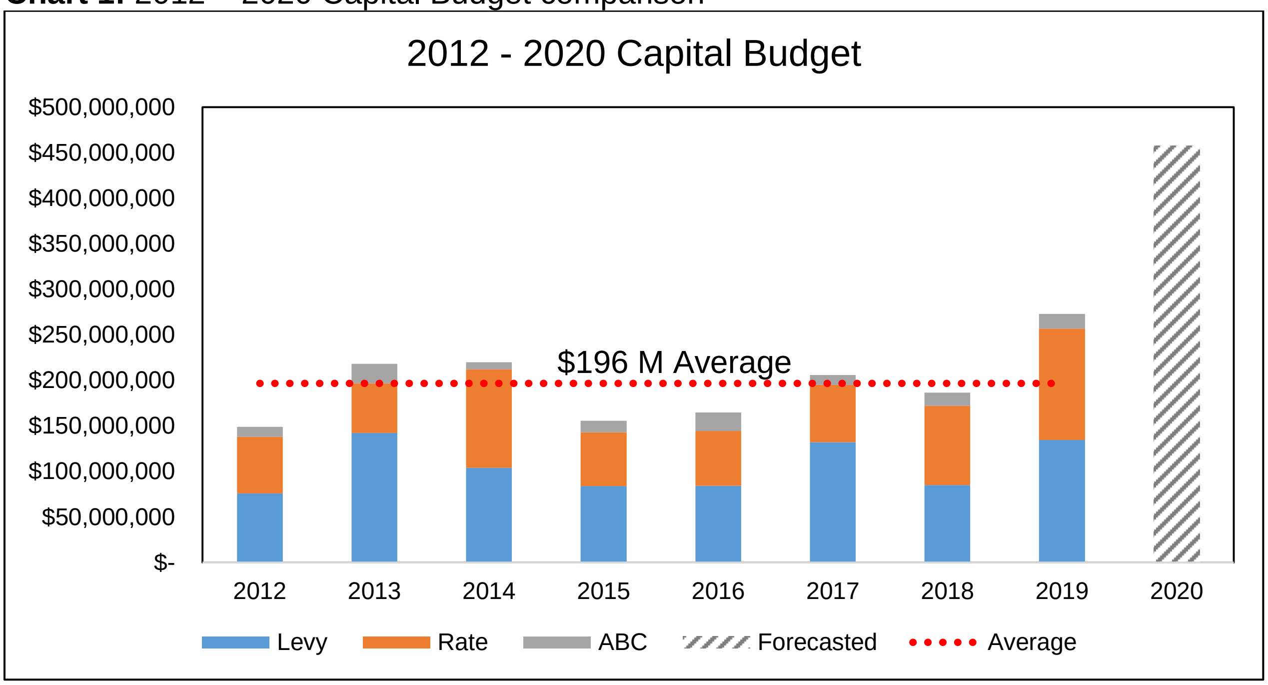
[1] **On January 17 2019 Council approved CL-C-2019 – NRH-2-2019 which initiated the project J_200001031.**

- Niagara Regional Housing budget has been approved by the Board. Niagara Regional Police Services Capital Budget is a draft subject to board approval on January 16th.
- **This report was revised to accommodate for the Project J_20001038: Transportation Infrastructure Means Protection following the recommendations from PHD 03-2019 and BRC-C 1-2019.**

Financial Considerations

The proposed 2019 Capital Budget of ~~$273.94~~ **$274.28** million (~~$151.59~~ **$151.93** million levy capital budget and $122.35 million rate capital budget) is included in Appendix 1. The 2019 capital budget is the Region's largest request to date.

Chart 1: 2012 – 2020 Capital Budget comparison



The 2019 Capital Budget being presented is fully funded as a result of the following:

- Review of existing projects to either reduce budgets or close projects. These efforts totaled to $8 million from 35 projects.
- Use of capital reserves, including drawing down the General Capital Levy and Infrastructure Deficit Reserve
- Increase in gross debt charges of no more than 2% per year, in order to balance the impact of debt charges on the operating budget (subject to Council's approval).
- Total consolidated authorized debt (Regional and Local), throughout 2019 and forecast period, to remain below 118% of Niagara Region's operating revenues. If the ratio of issued debt to operating revenue surpasses 120% or total consolidated debt surpasses $1 billion (determined by Standard and Poor's (S&P)), there is a risk of downgrade in the Region's credit rating.
- The total debt charges, throughout 2019 and forecast period, are projected to remain below 11% of the Niagara Region's own source revenues based on forecasted debt issuances. The maximum ratio of debt charges to own source revenue (annual repayment limit – ARL) set by the Province is 25%.
- Debt financing is applied to projects/assets that have a longer life span (i.e. 30 years). Debt terms do not exceed the expected useful life of the asset.
- Maximizing the usage of the development charges for growth related projects.
- Departmental leadership in collaboration with the Corporate Leadership Team also reviewed the 2019 capital request and prioritized projects based on criteria such as: alignment to AMP, supporting growth, council priorities, project risk, operating benefits and ability to leverage external financing.

A reconciliation to incorporate the recommendations of PHD 3-2019 and BRC-C 1-2019 are as follows:

Description	Gross Request	Reserve	Development Charges	Debt, Federal Gas Tax and other
Original Gross Request	$273,939,966	$132,387,466	$57,031,300	$84,521,200
Deferral and reductions:				
J_20000929 Geneva/Carlton	(1,000,000)	(500,000)	(500,000)	-
J_20000927 Thorold Yard Upgrades	(1,500,000)	(960,000)	(540,000)	-
J_20000912 Roads Resurfacing	(1,156,000)	(1,040,000)	(115,600)	-
Additions				
J_ 20001038 Transpt. Infra. Means Prot.	4,000,000	4,000,000	-	-
Revised Gross Request	**$274,283,966**	**$133,887,066**	**$55,875,700**	**$84,521,200**

The funding sources for the Capital Budget are shown in Table 1.

Table 1: 2019 Capital Funding Sources

	Levy	Rate	Total
Regional Funding:			
Reserves*	~~$ 44,627,066~~		~~$128,678,466~~
	$ 46,126,066	$84,052,400	**$130,179,066**
Infrastructure Deficit Reserves	3,708,000		3,708,000
Debentures	27,774,804	33,110,000	60,884,804
	~~77,109,870~~		~~193,272,270~~
	77,609,470	117,162,400	**194,771,870**
External Funding:			
Area Municipalities	3,025,000		3,025,000
Federal Gas Tax	10,300,000	3,000,000	13,300,000
Other External	2,511,396	4,800,000	7,311,396
	15,836,396	7,800,000	23,636,396
Development Charges	~~38,469,200~~		~~57,031,300~~
	37,313,600	18,562,100	**55,875,700**
Total	~~**$130,415,466**~~		~~**$273,939,966**~~
	$130,759,466	**$143,524,500**	**$274,283,966**

* The environmental centre expansion project, $21.17M is a project managed by the Facilities division but funded by the Rate programs

The budget provides for the full cost of the projects however actual cash flows may extend over multiple years. The operating budget impact of the 2019 Capital Budget is provided for at the time the capital budget is approved. This is to ensure that no capital project approved in one year will pre-encumber a future budget year or Council. For projects that include debt as a funding source, it is necessary for the operating budget to support the implied debt charges (interest and principal payments) at the time of capital budget approval. Debt financing is not issued until the project is substantially complete which may create a timing difference and any resulting variance is held in the capital levy reserve. The timing differences present an opportunity to reinvest these capital levy dollars in future infrastructure.

9 Year Forecast Financing Strategy

Key assumptions used in building the 2020-2028 forecast include:

- Interest rates on issued debentures averaged 3.20% for the July 2018 25-year debenture issuance. Interest rate assumptions used in the forecast are based on the general economic forecast that interest rates will begin to rise from a low of 2.5% for 5-year debt in 2019 to a high of 5.25% for 30-year debt in 2028.
- The 10-year Water and Wastewater financial plan prepared to comply with the Safe Drinking Water Act which requires a combined rate increase of 5.20% per year.
- Significant use of capital reserves as shown in the forecast of capital reserve balances in Appendix 5.

The current 10-year infrastructure deficit is estimated at $481 million. The forecast does not assume the usage of debt to fund the infrastructure deficit. This amount changes every year due to the timing of projects and new funding assumptions.
Some examples of changes from the prior year forecast are:

- The 10-year Water and Wastewater financial plan will utilize $112 million of debt to address the Municipal water licensing program
- External grant funding estimated at $80 million required but unconfirmed for construction of new South Niagara Falls Wastewater Treatment Plant as per Master Plan.
- Forecasted future Long Term Care Campus of $98 million in 2028

Debt Strategy

Debt is an important capital financing tool to assist in funding capital projects. The projects that are being financed through $60.9 million in debt are shown in Table 2 and will be leveraging debt for the following reasons:

- Large project costs are spread out over their useful life
- Infrastructure costs will be paid by future beneficiaries of the asset
- Historical budget increases for reserve contributions to sustain existing infrastructure have not been adequate.

Table 2: 2019 Debt-financed Projects

Project	**Debt**	**Funding**	**Council Priority**
Niagara Regional Transit	$11.9 million	Separate levy	Moving People and Goods
Water and Wastewater Infrastructure	$33.1 million	Within guidance	Advance Organization Excellence
Niagara Regional Housing	$10.2 million	Within guidance	Building a Labour-ready forecast
Various Bridge Reconstruction	$5.7 million	Within guidance	Moving People and Goods
Total	$60.9 million		

Debt financing of $60.9 million is proposed to balance the 2019 Capital Budget. The impact of the request will place Niagara below the average of comparable Regions in 4 of the 6 debt metrics identified in Table 3. The information on the Financial Information Return below represents actual debt issued with the exception of the S&P ratio.

Table 3: Debt Metrics

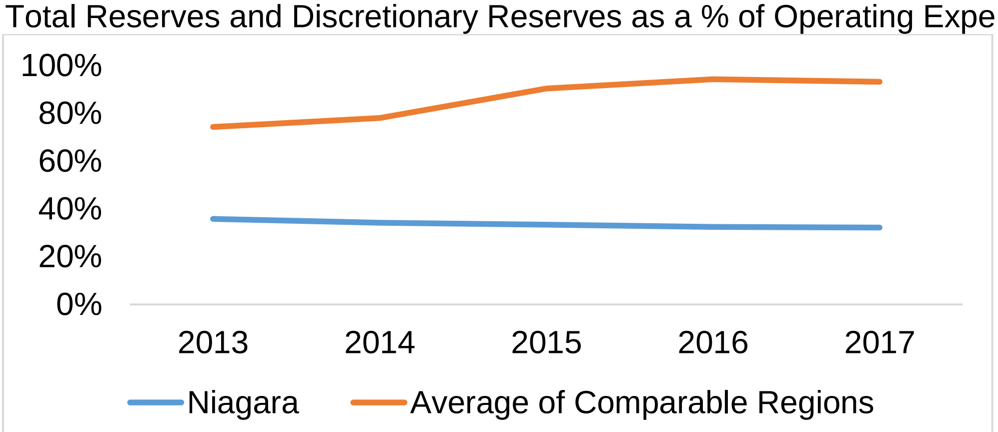
Metric	Current State	Proposed with 2019 Budget	Average of Comparable Regions*
Debt as a % of Operating Revenues	37.0%	44.0%	57.0%
Debt as a % of Reserves & Reserve Funds	86.0%	101.0%	85.0%
Debt per Capita	$ 754.95	$ 887.63	$ 1,148.51
Debt per Household	$ 1,742.96	$ 2,049.28	$ 3,553.93
S&P Ratio of Total Region and lower tier Debt to Operating Revenue**	81.0%	89.0%	70.5%
Annual Repayment Limit (ARL)	8.0%	8.0%	9.3%

Source: Ministry of Municipal Affairs Financial Information Return
* The comparable regions are Durham, Halton, Peel, York and Waterloo
**Waterloo does not use S&P as their credit agency and thus was not included for this analysis

Reserve Strategy

Each year the Ministry of Municipal Affairs and Housing reviews a number of financial metrics for all municipalities. One of these metrics is "Total Reserves and Discretionary Reserves as a % of Operating Revenues". Chart 2 demonstrates that Niagara Region's reserve levels are lower than its provincial comparators. Niagara Region has maintained its reserves at relatively the same levels for the six-year period from 2013 to 2017 therefore the use of debt to finance capital is necessary to support our asset management plan. The forecasted 10-year reserve balance is provided in Appendix 5.

Chart 2: Total Reserves and Discretionary Reserves as a % of Operating Expenses



Source: Ministry of Municipal Affairs Financial Information Return
* The comparable regions are Durham, Halton, Peel, York and Waterloo

1% Infrastructure Deficit Reduction Reserve

As part of the 2017 budget, Council approved the creation of an Infrastructure Deficit Reduction (IDR) reserve through a 1% increase on the levy. The establishment of the IDR reserve was the first step in a long-term capital financing strategy to reduce the infrastructure funding gap. In accordance with the requirements of the Asset Management Plan (AMP) discussed below, the Region is proposing the use of the IDR reserve as a funding source of the 2019 Capital Budget. To support growth in the region, staff recommends using the IDR to fund the Region's share (non-growth related portion) on projects as provided in Appendix 6.

Analysis

The proposed projects in the 2019 Capital Budget are based on information contained in the Asset Management Plan, updated based on current condition assessments, age-based analysis, employee identified concerns, current service standards and the Transportation Master Plan, Water Wastewater Master Servicing Plan, and Municipal Comprehensive Review and staff capacity to complete current and previously approved projects.

Supporting Growth

In the 2019 Capital Budget, ~~$57~~ **$56** million or 20.9% of the gross request has been identified as growth related eligible to be financed through development charges (DCs) under the current DC background study. The 5-year historical average of DC usage has been approximately $20 million. The 10-year forecast will be utilizing on average $47 million. Based on the current projection Wastewater development charge reserves will be fully utilized over the forecast period. This is reflective of the investment in growth. The following projects supporting job creation and attraction of new residents are funded with development charges:

Table 4: Highest Growth projects

Project	Gross Budget	Population Affected and Job's created	Supports GO
Martindale Road Reconstruction*	$16.1 million	4,200	Yes
Casablanca Boulevard Widening*	$10.0 million	6,620	Yes
Grimsby Water Treatment Plant System Storage	$11.5 million	38,400	No
Thorold Stone Road Extension*	$6.0 million	3,010	Yes

* Source: St. Catharines Secondary Plan, Grimsby Secondary plan and the Niagara Falls Station Area plan

Status of Previously Approved Capital (Work in progress)

Each years' capital budget request is cognizant of the capacity and resources available to manage both the existing capital projects as well as those proposed. Due to the multi-year nature of many capital projects there is always some approved capital budget for future year cash flow of the projects as noted below however the unspent amount is relatively stable reflective of an average three year life cycle for large capital projects from design through to construction completion. The increase in 2018 is related primarily to a number of large water and wastewater projects that were delayed for a number of unforeseen circumstances however significant progress has been made in Q4 of 2018.

- Q3 2018 – 37% budget remaining on $1,116 million approved budget
- Q3 2017 – 33% budget remaining on $1,053 million approved budget
- Q3 2016 – 30% budget remaining on $926 million approved budget

The above prior year budgets would have included budget estimates for the NRPS D1 Facility and Burgoyne Bridge projects. Additional forthcoming requests as described in the following report~~s~~ have not been included in the proposed 2019 Capital Budget as they are anticipated to be accommodated through the Capital Variance Project:

- CSD 13-2019: Niagara Regional Police Services 1 District Facility requesting $3,795,841
- ~~PHD 3-2019: Burgoyne Bridge requesting an additional amount to be determined for safety barriers~~

Staff continue to review existing projects on a quarterly basis for timely closure and/or identification of excess funding. In addition, there has been collaboration with the Project Management office to implement project best practices and techniques across the organizations.

Asset Management Plan

In 2017, the Region completed and Council approved a comprehensive Asset Management Plan. This AMP is a long range planning document that supports the Region's vision and priorities to sustain Niagara's infrastructure.

The detailed information available in this AMP was utilized in the 2019 budget cycle to validate all proposed capital projects identified as the replacement of existing assets, as summarized in Appendix 7. In the current year, 60% (2018 – 49%) of the projects are directly attributable to the AMP.

The AMP identified a $73 million annual gap between what the Region's 10-year capital budget plan and the required investment to sustain the Region's assets.

The $73 million annual gap was mainly caused by Water and Wastewater's asset portfolio and will be addressed in the 10-year Water and Wastewater financial plan. In order to alleviate pressures on the rate from the AMP, the plan will spread the backlog of projects over 50 years and propose a funding strategy.

Risks

The risks associated with the proposed capital and financing strategy are:

- Increasing use of debt and reserves will result in an increase in the Region's net-debt position. This may reduce the Region's financial flexibility and could lead to higher borrowing costs.
- Any use of regional sources of funding to growth related projects further erodes the ability to sustain the service level of current infrastructure.
- The Region retained an external project management consultant, which provided a detailed analysis on assessing the ability of current project managers and support resources in select departments. One of the finding was that divisions do not have adequate labour resources to complete open projects. There is an ongoing project with the development of the Project Management Centre of excellence to address this finding.
- The Region continues to increase the alignment of the Capital budget with the asset management plan. If the Region deviates from the asset management plan, this may result in deferred investment, equipment failure, reactive capital spending and higher costs.

Alternatives Reviewed

No alternatives were reviewed.

Relationship to Council Strategic Priorities

The 2019 Capital Budget supports an environment that contributes to economic prosperity. See Appendix 8 for a list of projects aligned to Council's Strategic Priorities summarized as follows.

- *60%* - investment in organizational excellence is primarily focused on the sustainment of existing infrastructure and service levels.
- *34%* - investment in moving people and goods is focused on the creation of new infrastructure to support growth and provide additional capacity and enhancements to the existing levels of service.
- *5%* - investment in building a labour ready workforce and is focused on increasing access to affordable housing which is an important factor in obtaining employment.

Other Pertinent Reports

AC-C 22 – 2018	Regional Debt Risk Management Framework
BRC-C 1 -2019	**Funding for Barriers**
CSD 21 – 2017	Asset Management Plan
CSD 35 – 2018	2019 Budget Planning
CSD 36 – 2018	PM Resource Assessment Report
CSD 51 – 2018	Asset Management Governance
CSD 63 – 2017	Regional Development Charges and Proposed By-law
PDS 37 – 2016	Niagara 2041 Growth Strategy - Local Municipal Growth Allocations
PHD 3 – 2019	**Preventing Deaths by Suicide on Public Infrastructure**
PW 22 – 2017	2016 Water & Wastewater Master Servicing Plan Update
TSC-C 3 – 2017	Niagara Region Transportation Master Plan

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Appendices

Appendix 1 **REVISED** 2019 Capital Budget Summary by Department with Funding
Appendix 2 **REVISED** 2019 Capital Projects Initiated Concurrent with Budget Approval
Appendix 3 2019 Capital Projects for Future Initiation
Appendix 4 **REVISED** 2019 – 2028s Capital Budget and Nine Year Forecast
Appendix 5 Forecasted Capital Reserve Balances
Appendix 6 Projects Allocated 1% Infrastructure Deficit Reduction Funding
Appendix 7 **REVISED** Alignment with the Asset Management Plan
Appendix 8 **REVISED** Alignment with Council Strategic Priorities
Appendix 9 Treasurer’s Certificate