RESERVES AND DEBT MANAGEMENT

As approved on January 31th, 2023

Reserves and Debt Management

The Fiscal Strategy includes four pillars to ensure long-term financial sustainability. The previous two sections of the budget addressed Revenue Management and Capital Planning, while this section focuses on the Reserve Management and Debt Management pillars. Balancing the use of reserves and debt must be carefully managed in the 10-Year Capital Plan. Reserve contributions and draws (both capital project funding and debt repayment) must be considered when developing the plan. This section explores that balance further.

Reserve Management

Reserves are used to fund capital projects and manage fiscal shocks to the Operating Budget. Reserves are funded through a number of sources including:

- Planned Operating Budget contributions to reserves funded through the tax levy or user rates
- Grants received from the provincial or federal governments
- Development charges and other development revenues collected for growth
- Operating Budget surpluses which are allocated based on the Council approved surplus management strategy.

The Operating Budget fiscal shocks are managed with stabilization reserves

In the Operating Budget, reserves are used to manage fiscal shocks to the budget which could result in large swings to the tax levy or user rates. This is done by smoothing the contributions to capital reserves and through the tax rate stabilization reserve or user rate reserves.

A standard practice is to keep the tax stabilization reserve at a target balance of about 10 percent of annual tax revenue to pay for any unforeseen pressures. The tax stabilization reserve will be used over the period of 2023 – 2026 to phase in the incremental operating cost required for the new financial system.

Forecasted reserve balances

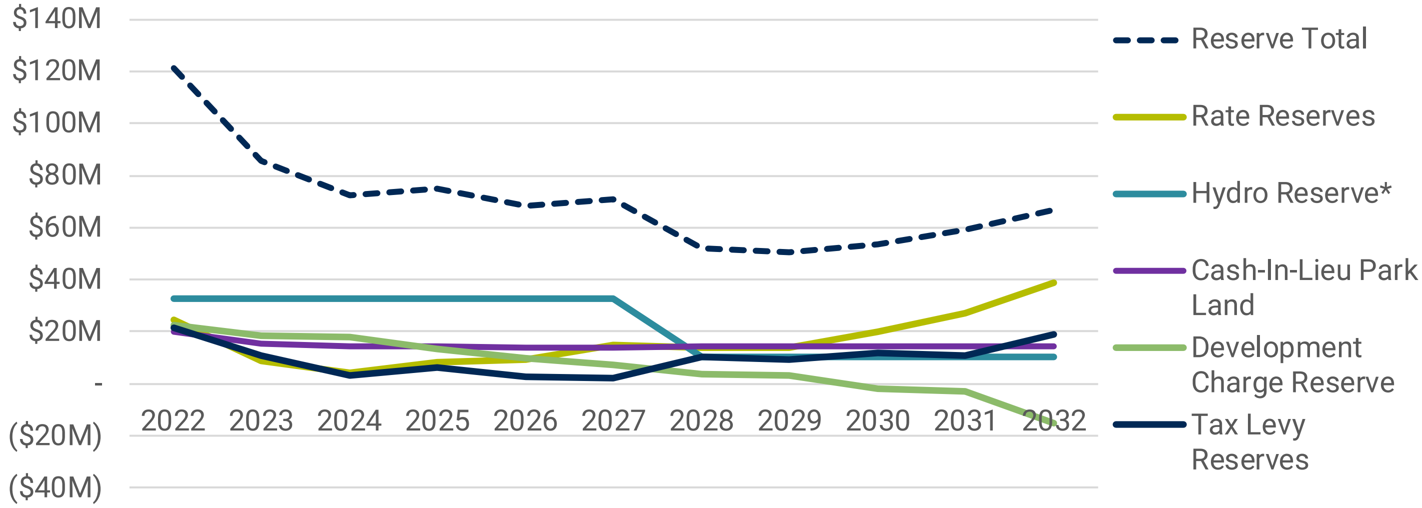
($M)	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
Tax Levy Funded											
Rehab & Replacement											
Roads	7.5	3.1	(4.2)	(2.2)	(1.1)	(3.4)	(0.2)	(2.9)	(5.9)	(4.6)	3.3
Facilities	4.6	2.9	3.6	3.6	1.9	2.9	3.1	3.6	4.5	5.1	6.4
Information Technology	0.6	(1.1)	(0.9)	(0.7)	(0.3)	0.4	1.2	2.1	3.1	4.1	5.3
Fleet	3.0	3.0	3.1	3.2	1.9	1.3	2.2	3.0	3.0	3.7	4.0
Parks & Recreation	2.4	1.7	1.3	1.4	0.3	0.9	1.5	1.6	2.1	2.5	3.9
	18.1	9.6	2.8	5.3	2.8	2.0	7.9	7.4	6.8	10.7	22.8
Growth & New	2.7	1.3	0.6	1.1	0.2	0.1	2.6	1.8	4.8	4.2	4.0
Studies & Other	0.7	(0.3)	(0.4)	(0.3)	(0.3)	(0.1)	(0.3)	0.0	0.0	(0.0)	0.3
	21.5	10.6	3.0	6.0	2.7	2.0	10.2	9.2	11.6	14.8	27.2
Rate Funded											
Water	11.6	7.7	7.1	8.8	11.0	13.5	16.2	19.1	22.5	26.0	29.8
Wastewater	4.4	3.4	4.3	5.3	6.6	8.0	9.5	11.1	12.9	14.8	16.8
Stormwater	8.7	(2.5)	(7.0)	(5.6)	(8.6)	(6.5)	(11.7)	(16.4)	(15.6)	(13.5)	(7.9)
	24.7	8.6	4.4	8.4	9.0	14.9	13.9	13.8	19.8	27.3	38.7
Development Charges											
Fire Services	(2.4)	(2.2)	(3.0)	(4.7)	(5.1)	(5.0)	(4.8)	(4.7)	(5.4)	(5.2)	(5.1)
Roads & Related	13.6	13.3	13.8	14.0	12.8	12.7	10.4	11.1	9.1	7.8	(4.4)
Parks & Recreation	6.2	2.3	1.8	(0.9)	(3.2)	(4.5)	(5.9)	(7.6)	(10.4)	(11.2)	(11.9)
Library Services	1.7	2.0	1.7	1.4	1.1	0.8	0.5	0.6	0.8	1.0	1.2
Water Supply & Distribution	1.2	1.3	1.4	1.5	1.6	1.7	1.8	1.9	2.0	2.1	2.2
Sewer	1.4	1.6	1.8	1.8	2.0	0.7	0.8	1.0	1.2	1.3	1.5
General Government	0.3	(0.3)	(0.1)	0.1	0.2	0.4	0.5	0.3	0.4	0.6	0.8
Municipal Parking Spots	0.4	0.4	0.3	0.3	0.3	0.4	0.4	0.4	0.4	0.4	0.4
	22.3	18.4	17.7	13.5	9.7	7.1	3.5	3.0	(1.9)	(3.2)	(15.4)
Cash-In-Lieu Park Land											
Cash-In-Lieu Park Land	19.8	15.2	14.5	14.3	13.8	14.1	14.3	14.3	14.1	14.1	14.1
Hydro Reserve											
Hydro Reserve	32.9	32.9	32.9	32.9	32.9	32.9	10.1	10.1	10.1	10.1	10.1
Total	**121.3**	**85.6**	**72.5**	**75.2**	**68.2**	**71.0**	**52.1**	**50.4**	**53.7**	**63.2**	**74.8**

Reserves are used to fund capital projects

Capital projects in the 10-Year Capital Plan are funded from reserves. There are a number of reserves that are used to fund capital projects and the funds are applied to the project based on the purpose for which each reserve can be used. The table above shows the balance of these reserves over the next 10 years.

The tax-funded reserves maintain a healthy balance after the elimination of $19.9-million worth of roads projects from the 10-Year Capital Plan. While development charge funded reserves do go into a negative balance, the overall capital reserves balance stays positive in all years.

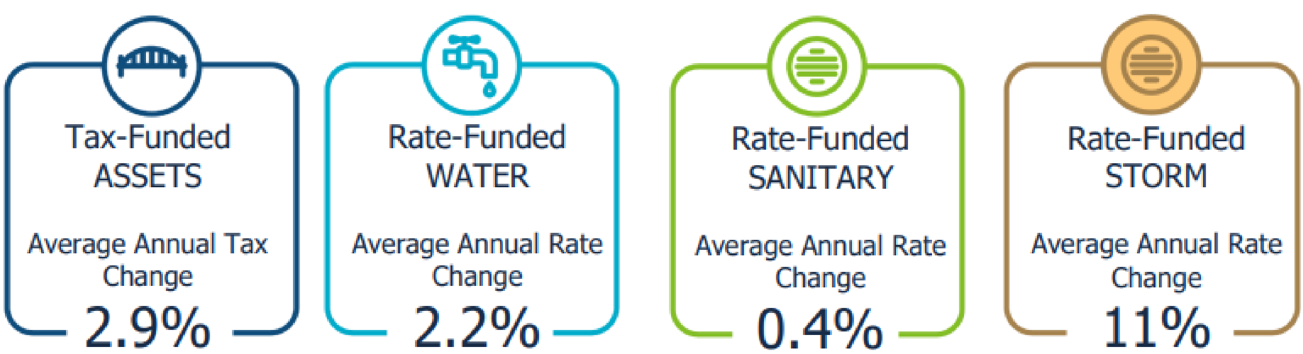
10-year capital reserves balances grouped by funding source



The second-generation asset management plan highlighted the need for higher reserve contributions

The second-generation asset management plan identified the need to further increase reserve contributions on an annual basis for the next 20 years to address a long-term infrastructure asset management funding gap. The funding gap was based on each asset's accounting estimated useful life. The next phases of the asset management plan will base asset replacement needs on approved service levels which need to be established by July 1, 2025. This additional work will refine just how big the funding gap is, and while it could reduce this gap, it will not eliminate it. The following shows annual tax and rate change recommended in the asset management plan to eliminate the infrastructure deficit for core assets based on a 20-year plan for tax funded assets, 10-year plan for water and wastewater assets and a 15-year plan for storm water assets.

Asset management plan recommended reserve increases by funding source



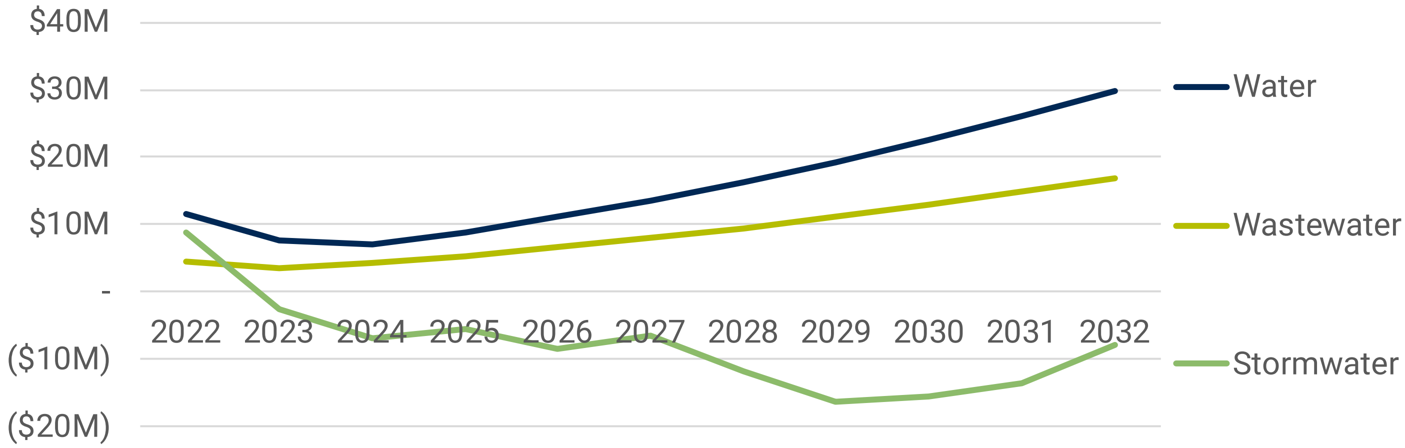
This Budget makes progress on filling the funding gap for user rate reserves

The user rate reserves are funded from the water, wastewater and stormwater rates. The reserve balances for water and wastewater are growing over this 10-year period. Most of Aurora's water and wastewater assets are relatively young as many have a lifespan of up to 80 years. The asset management needs for water and wastewater peak in the 2050s, providing time to save for the future, which is why growth in these reserve balances continues to be important.

However, the stormwater reserve does not have enough funding to support the existing short-term capital plan based upon current service level standards and before considering the longer-term asset management needs. The Budget includes a capital project for a stormwater rate study which will advise on the rates to be charged in the future to support the capital needs. This Budget includes the recommended annual incremental contributions to the rate-based reserves as outlined in the asset management plan.

The 2023 Budget proposes a water rate study project to develop a new water and wastewater rate model structure. The study will focus on fairness and certainty for reserve contributions and vacant homes paying their share, ensuring all customers pay regardless of consumption.

User rate funded reserve balances



Tax levy reserves are mostly used to support asset management

The Operating Budget includes capital reserve contributions which is part of the overall tax levy. This reserve contribution increases on an annual basis through the one percent tax levy increase to support the Fiscal Strategy. Most of these funds go to support asset management reserves, while the balance supports contributions to the growth & new and studies & other reserves.

The Budget includes increases to asset management reserves over 10 years

The Budget includes annual increases to asset management reserves. As the work on the asset management plan progresses, it is expected that the current practice of increasing asset management reserves with only a share of the one percent Fiscal Strategy levy increase will not be enough. Council will be presented with more information in 2023 to consider the impact of future asset management reserve contributions.

The 10-year plan and asset management plan show there is pressure to increase reserve contributions. This Budget assumes an increase of 0.25 percent annually starting in 2024 until the total contributions reach two percent of the tax levy in 2027. The proposed increase is a step forward but does not meet the requirements outlined in the asset management plan.

Inflation and limited funds resulted in projects being removed from the plan

To ensure the 10-Year Capital Plan is affordable, $19.9 million worth of roads projects, included in last years budget, were removed due to inflationary pressures and funding constraints, despite the assumed increase to asset management reserve funding starting in 2024. Removing these projects from the 10-Year Capital Plan may lead to increased cost pressures in the Operational Services operating budget in the next few years.

The following roads projects were removed from the 10-year capital plan:

- Reconstruction of Aurora Heights (PQI = 30) $6,871,500
- Reconstruction of Cousins Dr, Dunning Ave and Kennedy Street $1,463,800
- Vandorf Reconstruction (Leslie to 404) PQI = 35.4 $5,523,100
- Ridge Road Reconstruction (PQI = 30.8) $2,257,000
- Parking lot reconstruction Victoria and Temperance $1,064,500
- Reconstruction of Candac Valley, Alms Crt, Jarvis Ave. (PQI = 38.6) $2,675,800

To add these projects back into the 10-Year Capital Plan, a one-time levy increase of 3.7 percent would be needed in this Budget.

The tax levy also supports other capital reserves for growth and studies projects

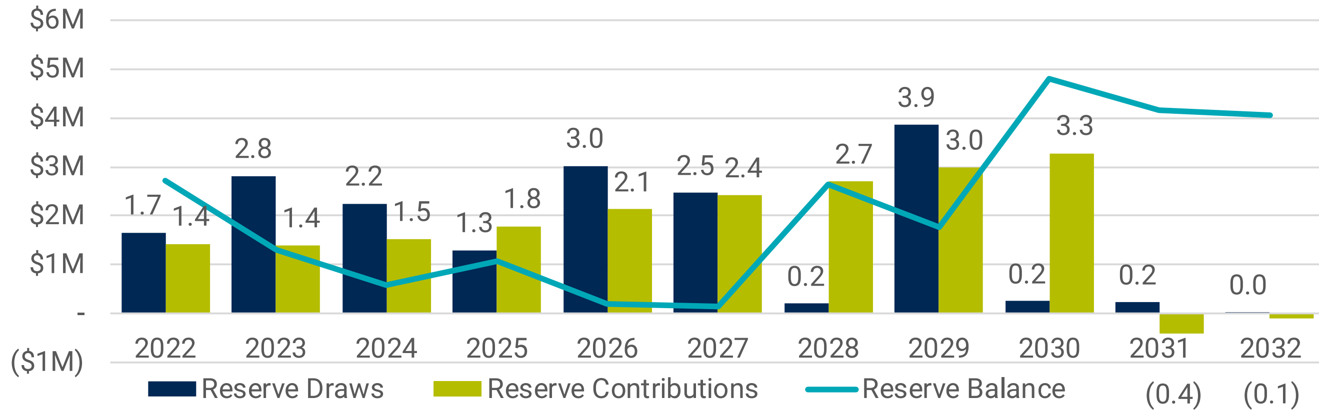
The growth & new reserve is used to pay for the non-Development and Community Benefit Charge funded portion of growth projects whereas the studies and other reserve supports strategic studies for both future capital and operating budget initiatives.

In 2022, supplementary tax revenue growth will be allocated to the growth and new reserve to pay for the tax funded portion of growth-related projects. The change in policy for allocating the extra supplementary revenue to this reserve was outlined in the 2022 year-end surplus/deficit management bylaw.

The construction of new recreation center (aquatic center) includes non-development charge funding including $4 million from the growth and new reserve. If this project does not move forward, the funds could be reallocated to use for roads asset management projects which were removed from the 10-year capital plan to make it affordable. Alternatively, the funds could be used to support other growth projects which may be no longer funded from development charges as a result of recent legislative changes.

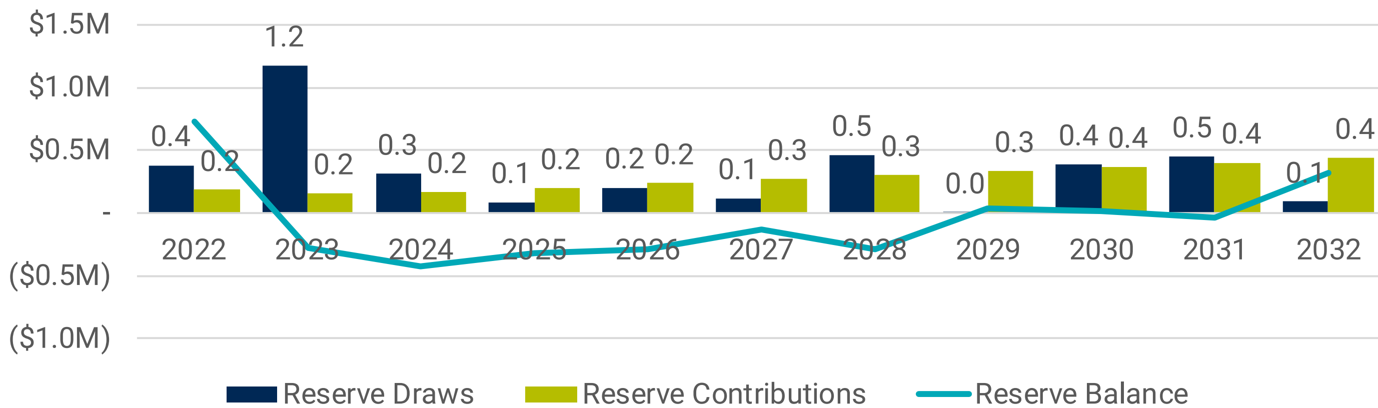
The new recreation center also impacts the development charge reserves and the impact of this is discussed further in the Debt Management portion of this chapter.

Growth and new 10-year reserve balances



The studies and other reserve are relatively small as it represents the smallest portion of the capital plan. The reserve has a few years where the balance dips negative but returns to a positive balance by the end of the 10-year capital plan.

Studies and other 10-year reserve balances



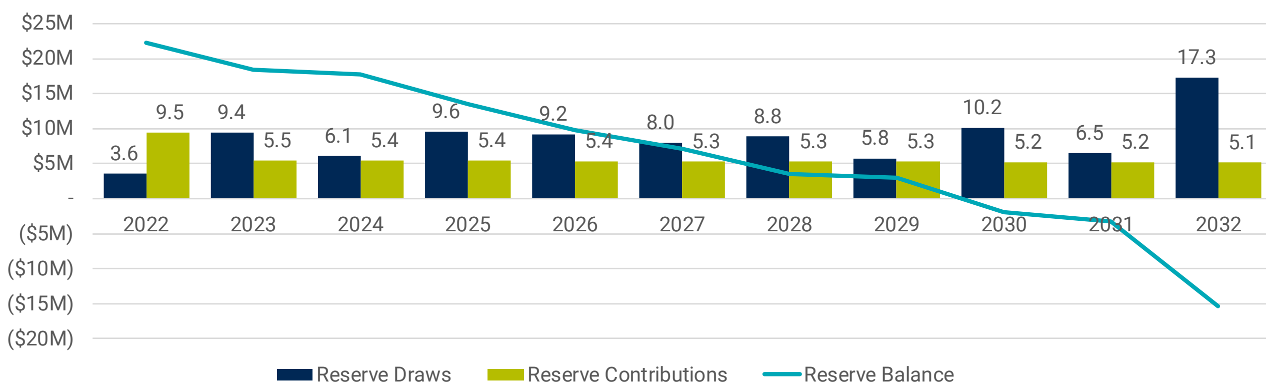
Development revenues are used to pay for growth

Development charges are collected on residential and non-residential developments and the new community benefit charges are collected on specific types of residential developments for the capital projects that are included in the studies and bylaws. These funds are used to pay for the growth-related costs of capital projects needed to maintain consistent level of service to a growing community. The calculation of these development revenues considers a number of factors:

- **Development charges** include any growth projects that have been identified in the study, the historical service levels for each category and any benefit to existing residents; these costs are then distributed over the projected growth period included in the study.
- **Community benefits charges** include the growth projects in the study and an appraisal of land value. The future growth is estimated and a maximum of four percent of the land value can be collected so long as the value of the projects meets or exceeds this amount. Note, the projects in this study cannot be included in the development charge study.

Over the last few years, development charge revenues were lower than what was forecasted in the 2019 Development Charge Study. The 2019 study forecasted that Aurora would receive $15.1 million on average over the five-year period from March 2019 to March 2024. The reserve forecast below shows that the contributions (development charge collections) are expected to continue to be lower than what was included in the study.

Development charge 10-year reserve forecast

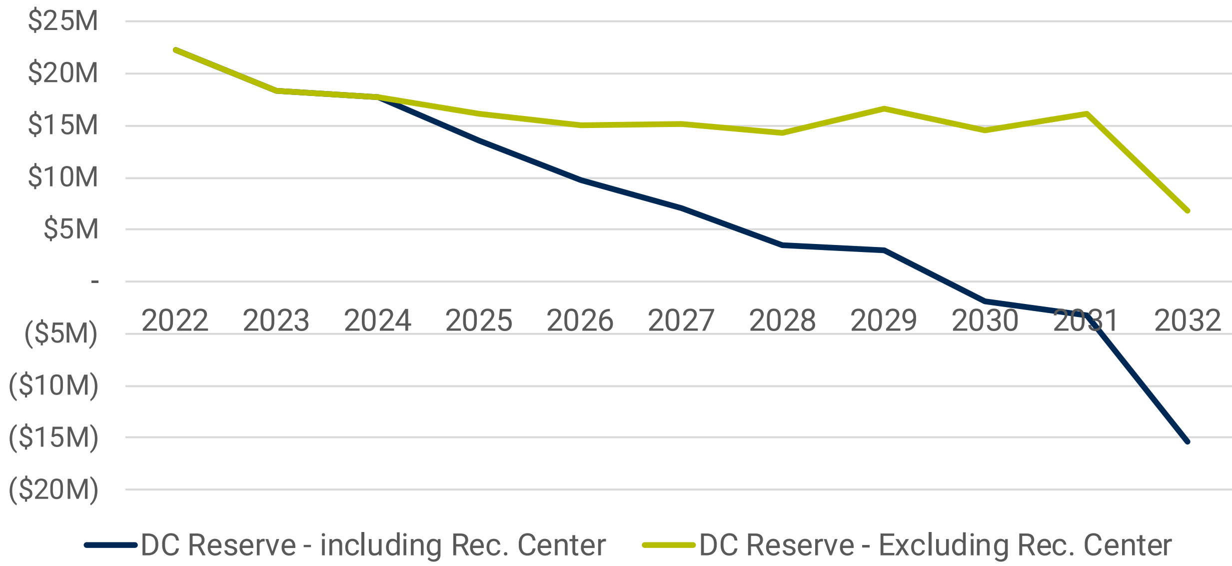


Changes are needed to future growth capital projects to ensure affordability

The development charge reserves dips into the negative balance beyond 2029 as the debt payments forecasted to pay for the new recreation center are significantly higher than the revenue collected through the development charges.

Currently, the development charge reserve forecast includes debt financing of the pre-COVID construction budget of $40.5 million for the new recreation center. Even with debt financing, the pre-COVID construction budget project is not affordable in this 10-Year Capital Plan.

Impact of the new recreation centre on the development charge reserve



The graph above shows the impact that the debt repayment costs for the new recreation centre project has on the development charge reserves over the next 10 years. This demonstrates that the project is not affordable and should not proceed with the construction unless alternative funding sources, such as grant revenue, are secured.

The removal of this project will also have an impact on the growth and new reserve of $4.1 million. If this project is removed from the 10-Year Capital Plan, these funds could be redirected to asset management or may be used to offset the impacts of proposed legislative changes that will impact future development charge collections.

Recent changes to the Development Charge Act will impact future revenues

On October 25, 2022, the Province of Ontario introduced Bill 23, More Homes Built Faster Act, 2022 in support of the More Homes Built Faster: Ontario's Housing Supply Action Plan: 2022-2023. The Bill, passed on November 28, 2022, amends a number of Acts, including the Development Charges Act, Planning Act, Conservation Authorities Act, as well as others. The legislative amendments will have significant impacts on the way municipalities plan, process and fund development. Historically, development charge revenue forecast considered for reserve analysis is very conservative compared to the much higher revenue projections mentioned in the current development charge study. However, material impacts to the municipality's development charge and other growth revenues due to these approved changes as it pertains to municipal finance are anticipated, such as:

- Removes some eligible capital costs such as studies that can be recouped through development charges
- The requirement to allocate at least 60 percent of the reserve funds in road, water and wastewater development charges and parkland cash-in-lieu.

- Development charge exemptions for the creation of affordable homes, reduced development charges for rental housing development and mandatory phase in of development charge rates bylaw. This is estimated to have minimum 3% tax levy increase implications to recover the lost development charge revenue
- Community Benefit Charge exemptions are proposed relating to affordable, attainable and inclusion zoning unit high density residential development. The impact on these revenues is not known at this time since the charge was only recently established
- Parkland revenues will be significantly reduced as the affordable and attainable housing units are exempt from parkland dedication units. This is estimated to have additional three percent tax levy increase in addition to lost development charge revenue

The full impact of Bill 23 on the Town's development charge revenue will be analyzed during the 2024 development charge study and bylaw update. The updated revenue projections will be reflected in the 2024 Budget and 10-year capital plan.

A reduction in development charges or other growth funding tools such as parkland dedication and community benefit charges will hinder the Town's ability to finance its growth-related infrastructure and put a greater burden on tax and ratepayers to fill this newly created funding gap. In the long-term, the total cost of home ownership will increase as homeowners pay higher property taxes and user rates to recoup the cost of growth-related infrastructure.

Debt Management

Debt is a financing tool which enables Aurora to manage the timing difference between when a capital project is constructed and when the funds are collected to pay for the project. This timing difference is most common for growth projects. Aurora's 10-year plan includes the repayment of debt issued for projects funded from development charges, user fees and the tax levy.

A new debt management policy will be considered by Council for approval in January 2023. The policy outlines the guidelines and controls for the issuance of debt including:

- A minimum balance of one-year's principal and interest costs shall be maintained in development charge reserves
- Debt funding source should be known at the time of debt financing
- Aurora's defined annual repayment limit and framework of debt

The 2023 Budget does not include any new debt authority to be approved by Council at this time. The 10-year capital plan assumes development charge funded debt will be issued to fund a sidewalk construction on Bathurst to Bloomington side road in 2026 and debt for the new recreation facility, which based on the new policy, is unaffordable.

Development charge debt considers affordability in the 10-year plan

Larger growth capital projects require significant funding from development charges. Development charges are collected over an extended period and often the project needs to be built in advance of growth.

New development charge funded debt should only be considered if the forecast can show that enough development charge revenues will be collected in the future to pay the debt principal and interest. The new debt policy will also recommend that a minimum balance of one year's principal and interest payments be maintained in the combined total of the development charge reserves. This Budget applies the principles of the new policy.

In applying the policy, the new recreation centre project was identified as being unaffordable in this 10-year plan funded from a combination of development charges (debt financed) and tax levy. The reason being is that even with using debt financing, the Town will not collect enough in development charges to repay the annual debt costs or maintain the one year's repayment costs.

This project could become affordable in the future if external funding, such as a grant, is received, once the current development charge debt is paid off and/or there is a sustained increase in development charge revenues in the future.

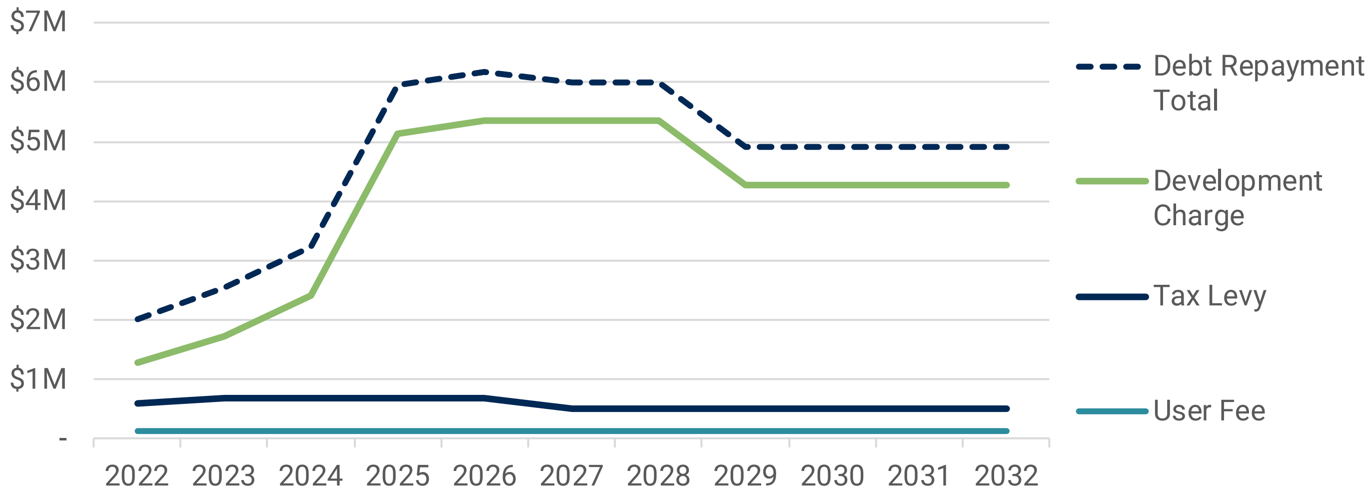
Existing debt is repaid through multiple sources

When debt principal and interest is paid, it is funded from the source that it would have used in the capital plan. The Town has debt which is currently funded from development charges, user fees and tax levy. Aurora's current outstanding debt includes:

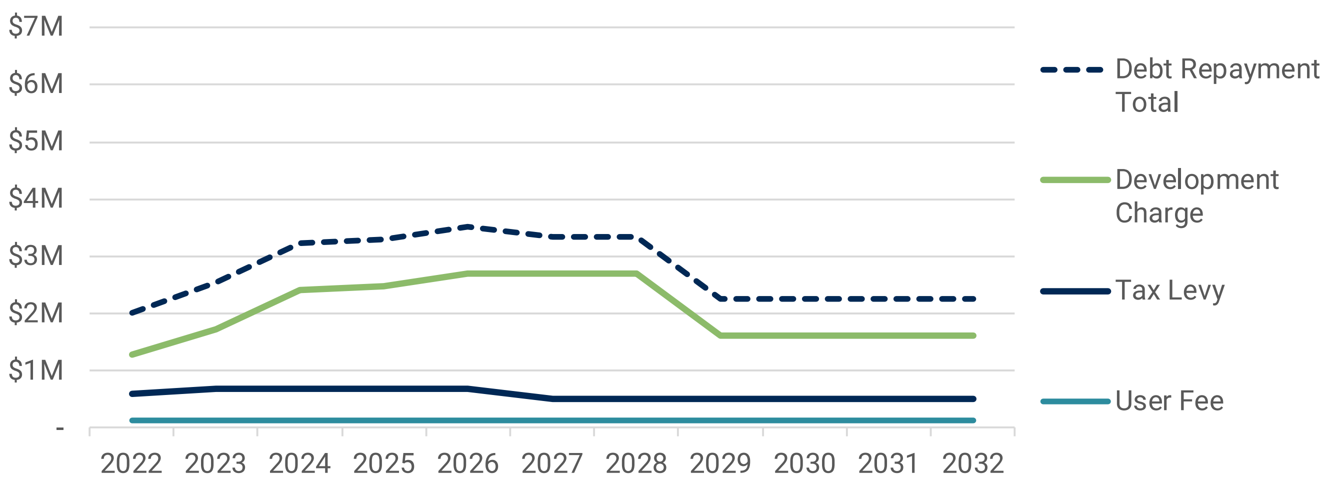
- Development Charge funded debt:
  - Stronach Aurora Recreation Complex: 20-year debenture which will be paid off in 2025
  - Joint Operations Centre: 10-year debenture which will be paid off in 2023
  - Hallmark Baseball Diamonds which will be paid off in 2041
  - The new gym at the Stronach Aurora Recreation Complex which is currently using a construction line of credit and expected to be converted to a 20-year debenture in 2025
- User fee funded debt:
  - Aurora Sports Dome: 15-year debenture which will be paid off in 2036
- Tax funded debt
  - LED Streetlight Conversion project which will be paid off in 2026
  - Aurora Town Square which is currently using a construction line of credit and will be converted to a capital loan in 2023 and long-term debt at a later date once interest rates decline.

When the debt repayment is completed for the two tax-funded projects, they will provide some relief on the tax levy. As part of the Fiscal Strategy, these funds used to repay debt will be converted to asset management reserve contributions.

Annual debt repayment costs by funding source including the new recreation centre



Annual debt repayment costs by funding source excluding the new recreation centre



Fiscal Strategy and financial policy ensure long-term financial sustainability

The Fiscal Strategy provides a long-term view to financial stewardship and financial management of Town resources. It ensures that the Town maintains desired service levels and adapts to the growth while managing the fiscal impacts year-over-year. In 2023, Council will consider a debt management policy which is aligned with Fiscal Strategy principles. Reserves and debt management pillars of the Fiscal Strategy supports the capital planning pillar of the Fiscal Strategy by managing the timing difference between when a capital project is built and when the funding for the project is received. Maintaining a positive reserve balance and manageable debt levels for the Town are the key indicators of long-term financial health. Reserves and debt graphs in this chapter show how fiscally sustainable decisions made during the budget approvals can ensure future financial health.

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