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Town of Aurora

General Committee Report

No. FIN23-001

Subject: Debt Management Policy

Prepared by: Sandeep Dhillon, CPA CMA, Senior Financial Management Advisor

Department: Finance

Date: January 17, 2023

Recommendation

1. That Report No. FIN23-001 be received; and
2. That the presented debt management policy for the Town be approved.

Executive Summary

This report highlights the significance of a debt management policy for the town's long-term financial sustainability and financial management. The policy ensures that the town maintains desired service levels and adapts to growth while maintaining moderate fiscal impacts from year to year. Acquisition of debt and debentures can play a very important role in the Town's finances. Debt can provide liquidity to fund new assets, infrastructure, and other capital projects when the asset is built in advance of growth. The Town should continue to use debt wisely over the long-term and understand that the prudent issuance of debt is an efficient use of available financial resources.

- The debt management policy supports the fiscal strategy objective of financial sustainability
- Debt Management Policy outlines the guidelines and controls for the issuance of debt
- The policy ensures that the debt financing is used responsibly
- The debt policy recommends an annual repayment limit of 10 percent which is lower than legislated

- Debt will be monitored with annual reporting as part of the budget and debt approval process

Background

Deft financing has been used to fund capital projects at the Town historically. In order to use debt wisely, the Town had established best practices that have guided historical debt management. These best practices include:

- Debt will only be considered as an interim financing source for capital projects when a funding source can be confidently assured for the repayment of the debt being considered.
- Debt could be considered when the asset is built in advance of growth.
- Debt can only be considered when the annual carrying costs remain under the provincially prescribed Annual Repayment Limit.

The Town has responsibly used both external and internal debt financing for several years as an interim financing source for necessary Town capital asset creation which has included indoor and outdoor recreation spaces, as well as library and cultural infrastructure. In all instances, all debt obligations were repaid on time. The development of the debt management policy is a recommended strategic action in the fiscal strategy to ensure longer term prudent financial and debt management.

Analysis

The debt management policy supports the fiscal strategy objective of financial sustainability

Issuing debt provides the flexibility to proceed with planned capital projects sooner than waiting to collect the funding source for the project in a reserve. Debt management pillar supports the capital planning and reserve management pillars 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. Debt management also supports revenue management as it provides Town the flexibility to borrow money at lower rate to finance capital projects and earn higher rate on return on Town's Capital asset reserve holdings.

Debt Management Policy outlines the guidelines and controls for the issuance of debt

The purpose of the Debt Management policy is to establish financial guidelines and appropriate controls for the issuance and management of debt for the Town of Aurora. This policy establishes objectives, standards of care, authorized financing instruments, reporting requirements and responsibilities for the prudent financing of the Town's infrastructure needs.

The objectives of the policy are outlined below:

- Adherence to Legislative Requirements
- Long-term Debt Financing
- Debt Financing Consideration Guidelines
- Ensure Long-term Financial Flexibility and Sustainability
- Aurora Debt Repayment Limit and Framework for Debt Management
- Limit Financial Risk Exposure
- Minimization of the Long-Term Cost of Financing
- Suitable and Authorized Debt Financing Instruments
- Financial Guarantees and Letters of Credit
- Notice Period
- Allocation of Excess Debt Financing to Capital Projects

The Town's current debt obligation remains in a healthy position

The Town's existing debt obligations are in a healthy position with all required funding for repayment being identified and assured. Table 1 presents a summary of the Town's current debt obligations as of December 31, 2021.

All the debt in Table 1 has been acquired through Infrastructure Ontario except the SARC construction debt which was acquired through York Region. The average rate of return on the Town's reserve funds investment over the last three years is 2.9 percent which is higher than the borrowing cost Town is paying on the debt through Infrastructure Ontario. The total annual carrying costs of this debt is 2.1 percent \$1,899,800, representing a value that is well under the Town's legislated annual debt repayment limit of \$23,130,500 (25% of own source revenue). When the approved short to long term debt conversions of \$10,000,000 and \$8,200,000, respectively for the Aurora Town Square and SARC Gymnasium projects are exercised the estimated total annual debt carrying costs will grow to 2.7 percent, \$2,928,000. This will reduce the available room in the annual debt repayment limit to \$20,202,500.

Table 1
Debt Financing Summary

	Length and Rate	Outstanding Principal	End Date	Repayment Funding Source(s)
Short Term Financing: Construction Line of Credit				
Aurora Town Square	Open 1.12%	15,338,000	Substantial project completion	Multiple funding sources, as per FIN20- 019.
SARC Gymnasium	n/a		Substantial project completion	Long term debenture financing.
Subtotal Short Term Financing		15,338,000		
Long Term Financing: Long-Term Debenture				
Hallmark Baseball Diamonds	20 years 2.65%	3,375,000	2041	Parks & Recreation DCs
SARC Construction	20 years 4.49%	1,164,737	2025	Parks & Recreation DCs
Aurora Sports Dome Purchase & Retrofit	15 years 2.42%	1,600,000	2036	Aurora Sports Dome annual operating revenues
LED Streetlight Conversion	10 years 2.29%	1,562,792	2026	Annual operating budget utility savings
JOC Construction	10 years 2.85%	3,749,277	2023	Parks & Recreation and Roads DCs
Subtotal Long Term Financing		11,451,806		
Total Debt Obligation		26,789,806		

The policy ensures that that the debt financing is used responsibly

Debt financing is a useful tool; however, consideration should be given to when debt should be acquired and when it should be not. For example, the borrowing cost on construction line of credit for Aurora Town square is 2% lower than the annual rate of return on hydro reserve funds. This results in a positive cash flow for the Town's overall financial management. Therefore, prior to the issuance of new capital debt financing, consideration will be given to the impact on Town's finances to achieve appropriate balance between debt financing and other forms of funding.

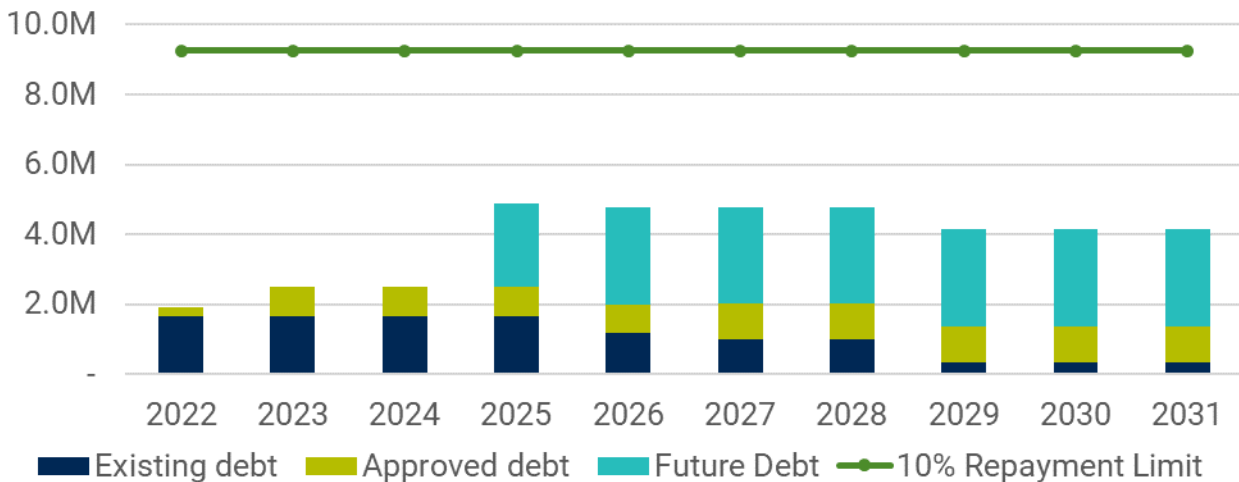
The debt policy recommends an annual repayment limit of 10 percent which is lower than legislated

The ARL is generally summarized as the maximum amount that a municipality in Ontario can pay each year (without first going to the Local Planning Appeal Tribunal) in principal and interest payments for long-term debt and other long-term financial commitments.

For most municipalities (not including Toronto and York Region) the ARL is set at 25 percent of their annual own- source revenues (such as property taxes, user fees and investment income), less their annual existing long-term debt service costs and payments for other long-term financial obligations. Municipalities may only exceed their ARL with the prior approval of the Local Planning Appeal Tribunal (LPAT). The Town's 2022 ARL is \$23,130,500 which has been calculated based on the data contained in the 2020 Financial Information Return.

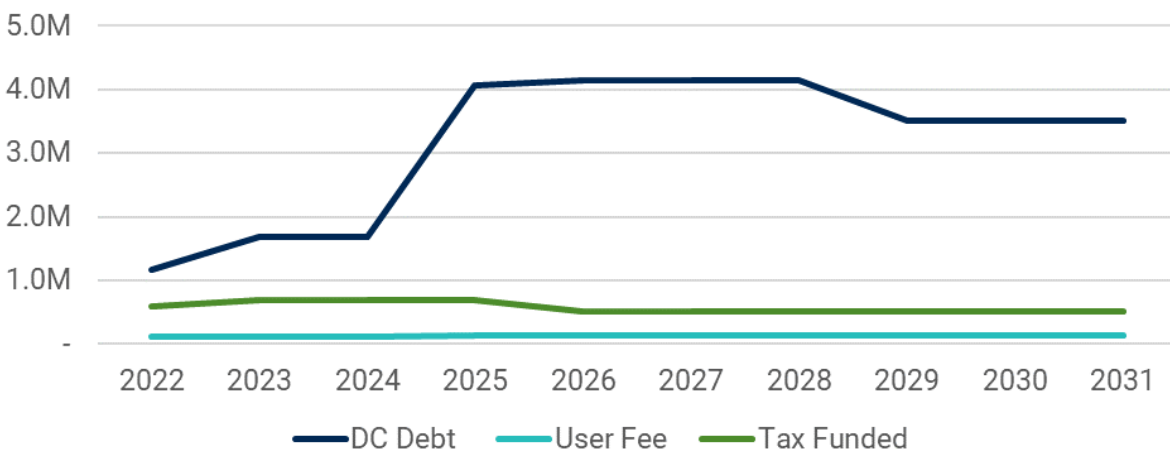
Issuing debt to the level prescribed by the province is not sustainable for the Town of Aurora. This policy sets a self-imposed ARL limit at 10% of own-source revenues. As per the Ministry of Municipal Affairs and Housing, Aurora's 2022 annual debt repayment cost is 2.1 percent of own-source revenue. When adding in the recent approvals of debt, annual repayment cost increase to 2.7 percent.

Figure 1
ARL vs. Debt Repayment Forecast



The policy recommends a lower ARL limit because much of Aurora's debt is funded from development charges (DC). Typically, the development charge revenues are collected over an extended period as the new developments are built. There is a risk of stranded debt in the instances when debt is issued based on provincial ARL target of 25% and the DC revenue forecast is much lower than the projected annual debt payments. Therefore, to be fiscally sustainable Town should not seek authority to exceed an ARL of 10% and for development charge funded debt, a minimum balance of one-year's principal and interest costs shall be maintained in the combined total of all DC reserves.

Figure 2
Annual debt repayments by funding source



Debt will be monitored with annual reporting as part of the budget and debt approval process

Another important component for the debt management policy is reporting and adherence to the policy. The implementation of the debt management policy principles in acquiring new debt should be monitored through the annual budget report and will be part of the reserve and debt management chapter of the budget binder.

Advisory Committee Review

Finance Advisory Committee reviewed the draft debt policy at its June 14th, 2022 meeting.

Legal Considerations

In accordance with Ontario Regulation 403/02: Debt and Financial Obligation Limits filed under the *Municipal Act, 2001*, S.O. 2001, c. 25, the Town is subject to the Annual Repayment Limit (ARL) of 25% of its own source revenues.

Financial Implications

There are no direct financial implications from this report. The financial implications will be in the budget as the policy is applied.

Communications Considerations

The Town will use “inform” as the level of engagement for this report and policy. The report will be placed on the Town’s website along with the Debt Management Policy.

Climate Change Considerations

The recommendations from this report does not impact greenhouse gas emissions or impact climate change adaptation.

Link to Strategic Plan

Debt Management Policy supports all aspects of the strategic plan. Specifically, this report supports the Plan principles of Leadership in Corporate and Financial Management, Leveraging Partnerships, and Progressive Corporate Excellence and Continuous Improvement.

Alternative(s) to the Recommendation

1. Council provide direction.

Conclusions

The debt policy provides the financial policy framework to ensure Aurora can set and stay on a financially sustainable path. This is done through by ensuring that the Town's fiscal impact year-over-year is manageable and is well below the Town's self-prescribed annual repayment limit of 10%. The policy also ensures that the Debt management pillar supports the fiscal strategy pillars of capital planning, reserve management and revenue management by managing the timing difference between when a capital project is built and when the funding for the project is received.

Attachments

Attachment 1 - Town of Aurora - Debt Management Policy

Previous Reports

FAC Memorandum, Debt Management Policy, June 14, 2021

Pre-submission Review

Agenda Management Team review on December 13, 2022

Approvals

Approved by Rachel Wainwright-van Kessel, Director, Finance

Approved by Doug Nadorozny, Chief Administrative Officer