

Optimal Reserve Balances

January 19, 2016
Presentation to Council

Project Objective

- Identify an optimal balance for each applicable reserve, based on a formula, as identified in FIN-001-024: Financial Reserves Policy to contribute to financial sustainability.
- Annually apply the formula and assess variances between the optimal balances and current balances. (Enclosure 4)
- Include recommendations to align current balances to optimal balances through the annual budget process and year-end surplus allocations.

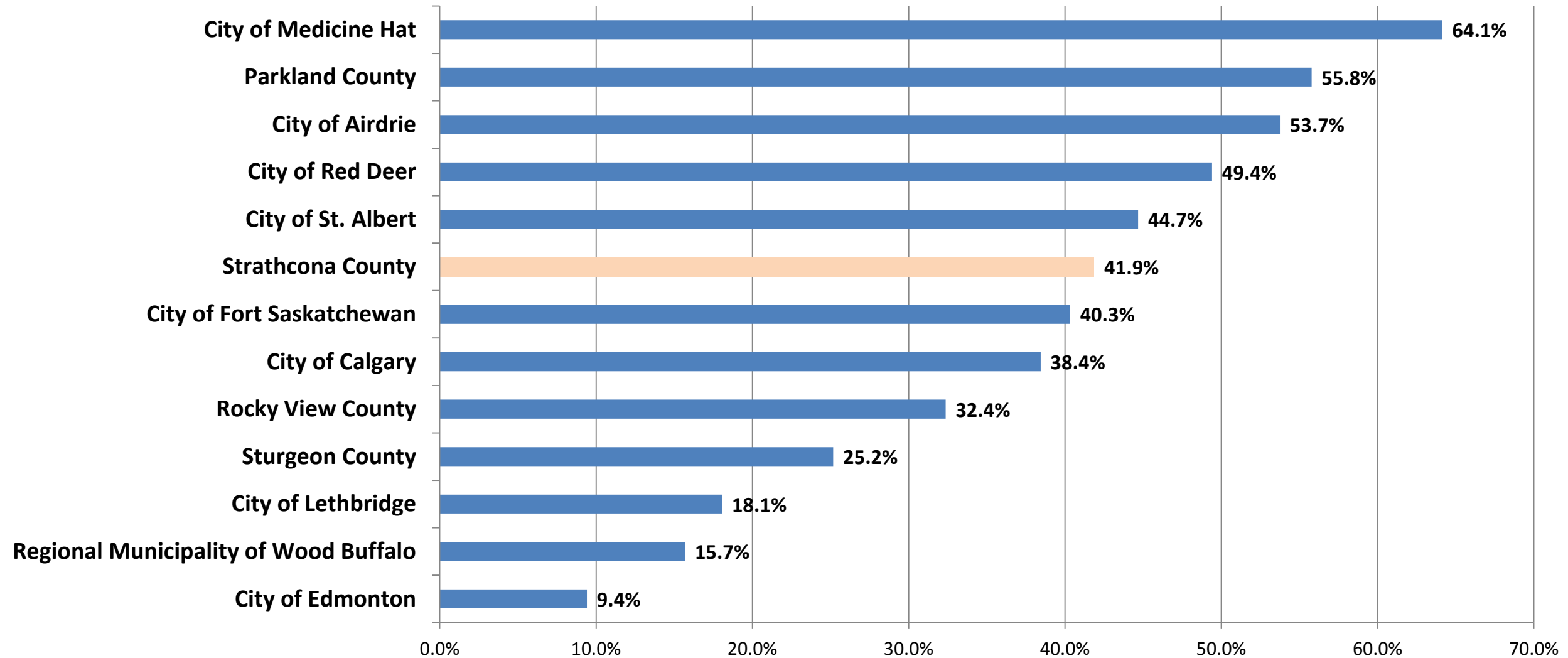
Considerations for Formula Development

- Reserve policy objectives and reserve purpose descriptions
- Government Finance Officers Association (GFOA) best practices
- Regional municipal practices and other Canadian municipal practices
- Internal operational forecasts and input
- Internal historical trend analysis regarding contributions and funding statistics
- Finance Advisory Committee and Executive Team advice

Comparative Reserves Information

Reserves Balances as a % of 2014 Operating Expenses and 2014 Capital Budget

Assumption: Reserves balances including committed and designated (uncommitted funds).



Source: 2014 Annual Reports for the individual Municipalities

Total Consolidated Reserves Overview

The total sum of the reserves balances is equivalent to:

- Approximately 42% of the 2014 Operating Expenses and 2014 Capital Budget

Justification

Maintaining a strong reserves balance allows Strathcona County to:

- Earn interest revenue on the cash balance
- Incur debt after construction is complete and costs are finalized minimizing the risk of over borrowing
- Reduce the amount of debt required to fund capital purchases
- Provide flexibility to address emergent issues and current priorities
- Balance intergenerational equity between current and future residents

Strathcona County continues to maintain reserves balances that are mid-range compared to other Alberta municipalities.

Municipal Reserves

Stabilization and Contingency Reserves

R1) Stabilization

Recommend a minimum balance equal to a 1% tax revenue increase

R2) Contingency

Recommend a minimum balance equal to 4% of municipal operating expenses

Justification

- Municipal Survey indicated majority of Municipalities reflect 5% as a minimum in their Stabilization and Contingency Reserve Category, which is in line with best practices.
- FINAC recommended the Stabilization and Contingency components be maintained as separate reserves.

Stabilization and Contingency Reserves

Municipal Survey		
Municipality	Have a stabilization reserve?	Is there a target or min/max?
Edmonton	Yes - Financial Stabilization Reserve	Min - 5% of tax-supported operating expenses, target is 8.3%
Calgary	Yes - Fiscal Stability Reserve	Min - 5% of tax-supported gross expenditures (net of recoveries), target is 15%
St. Albert	Yes - Stabilization Reserve	Ceiling is 2% of annual municipal operating budget
Airdrie	Yes - General Operating Reserve	Ceiling is 7% of annual operating budget
Saskatoon	Yes - Fiscal Stabilization Reserve	Min - 5% of current year's tax-supported expenditures
Regina	Yes - General Fund Reserve	Min - 5% of annual budgeted general operating revenues, Max is 10% of
Winnipeg	Yes - Financial Stabilization Reserve	Min - 8% of tax-supported expenditures

Municipal Projects Reserve

R4) Municipal Projects Reserve

Recommend a three part optimal balance formula:

Specific Project Allocations (current balance)

+

Capital Projects (historical percentage of capital projects funded from capital projects reserve applied to the five year capital forecast)

+

Operating Projects (five year historical average funded from fiscal projects allowance)

Justification

- This approach applies past trends to future forecasts and is sustainable based on budgeted contributions, potential surplus allocations, and development of future replenishment strategies.

Infrastructure Lifecycle, Maintenance & Replacement Reserve

R5) Infrastructure Lifecycle, Maintenance & Replacement Reserve

Recommend an average based on the 5 year forecast of annual infrastructure maintenance programs including operating and capital

Justification

- This provides funding equivalent to one year of annual infrastructure maintenance programs.
- This optimal balance is comparable to annual amortization expense
(2014 = \$38.0M)
- This optimal balance may be adjusted after the annual program review is complete.

Special Purpose Reserves

R9) General Land Reserve

Recommended optimal balance formula = 50% of forecasted 5 year land requirements

Justification

- This formula assumes a balanced approach to intergenerational equity by allocating equal funding from reserves and debt (typically the only two funding sources for land purchases).
- This optimal balance also aligns with the 5 year history of 2010-2014 spending for land projects (\$20.1M)
- This optimal balance formula may be adjusted upon completion of a land strategy and funding philosophy

Special Purpose Reserves Continued

R7) Strathcona Community Investment Program

As per Policy GOV-002-030, the maximum in this reserve cannot exceed 200% of the annual allocated amount, which is equivalent to \$200K

R12) Cultural Development Fund

Optimal balance yet to be determined

R13) Internal Financing

Optimal balance to be determined upon revision of FIN 002-025: Debt Management Policy

R15) Broadmoor Golf Course

Optimal balance yet to be determined

Municipal Reserves Optimal Balances

Stabilization	1.8	2.1	(0.3)
Contingency	7.7	9.8	(2.1)
Projects	20.7	22.3	(1.6)
Infrastructure Lifecycle, Maintenance and Replacement	24.3	31.9	(7.6)
Special Purpose and Other	11.8	14	(2.2)
Total Muni Reserves	66.3	80.1	(13.8)
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Utility Reserves

Utilities Reserves

RU1) Stabilization and Contingency

Recommend a minimum of 5% of utilities operating expenses

Justification

- Equivalent to municipal stabilization and contingency optimal balance formula

RU4) Utilities Infrastructure Lifecycle, Maintenance and Replacement

Recommend optimal balance equivalent to 5% of the future replacement cost of assets until completion of Utilities' financial policy

Justification

- Aging of costly utility infrastructure will need to be replaced in the foreseeable future
- This optimal balance formula will be adjusted upon completion of the Utilities' financial policy resulting from the Cost of Services Studies

Utility Reserves Optimal Balances

As at November 30, 2015 (in Millions \$)			
Utility Reserves	Designated Balance	Optimal Balance	Variance
Stabilization and Contingency	0.9	2.7	(1.8)
Projects	0	0	0.0
Infrastructure Lifecycle, Maintenance and Replacement	35	73.8	(38.8)
Special Purpose and Other	0	0	0.0
Total Muni Reserves	35.9	76.5	(40.6)

Reserve Policy Edits

(see Enclosures 1 & 2)

- Edit of Policy name from Municipal Reserves to Financial Reserves
- Edits to definitions for Optimal Balance and Reserve Description
- Edits to Guideline 8 describing Optimal Balances
- Addition of Schedule "A" – Optimal Balance Formulas
- Transition of Reserve Descriptions to Schedule "B"
- Restructuring of Internal Financing to a Special Purpose Reserve
- Creation of R7) Strathcona Community Investment Program and RU3) Utilities Projects Reserve Descriptions
- Edits to R8) Public Reserve Trust, 12) Cultural Development Fund and RU4) Utilities Infrastructure Lifecycle Reserve Descriptions
- Edits to Reserve Descriptions for Optimal Balances
- Collapsing R13) Rural Subdivision Approaches to merge with R5) Infrastructure Lifecycle Reserves
- Renumbering of Reserve Descriptions to align with additions and restructuring
- Other minor edits for clarification.

Re-designation of Reserve Funds

(see Enclosures 3)

Municipal

- \$1,366K from the Municipal Projects Reserve (1.3773) to the Infrastructure Lifecycle Maintenance and Replacement Reserve (1.3800).
- \$191K from the Rural Subdivision Approaches Reserve (1.3807) to the Infrastructure Lifecycle Maintenance and Replacement Reserve (1.3800).
- \$71K from the Council Priority Funds Reserve (1.3801) to the Strathcona Community Investment Program (1.3813)