The Regional Municipality of York

Committee of the Whole
Finance and Administration
March 11, 2021

Report of the Commissioner of Finance

2021 Regional Fiscal Strategy

1. Recommendations

1. Council adopt the updated fiscal strategy that is outlined in this report.

2. Council adopt the 2021 Long-Term Debt Management Plan, shown as Attachment 1 to this report.

3. Council adopt the resolution shown as Attachment 2 requesting the Province to:

    a. make changes to the *Development Charges Act* as outlined in this report to ensure that benefitting development fairly contributes to the cost of the Yonge Subway Extension

    b. renew the growth-related cost supplement component of York Region's Annual Repayment Limit that will expire on December 31, 2021

4. Council authorize the early repayment of $18,657,698 of tax levy and user rate debt originally due to be refinanced in 2021, from the following reserves:

Reserve	Amount
a. Debt Reduction Reserve	$ 8,714,376
b. Capital Asset Replacement – Water	$ 667,230
c. Capital Asset Replacement – Wastewater	$ 9,276,092

5. Council authorize the transfer of funds from the following reserves to YorkNet:

    a. Up to $1,203,570 of contributions that were previously made by YorkNet to the General Capital Reserve, to its Capital Asset Replacement Reserve; and

    b. Up to $459,976 of contributions that were previously made by YorkNet to the Tax Stabilization Reserve, to its Stabilization Reserve

6. The Regional Clerk circulate this report to Building Industry and Land Development Association - York Chapter

2. Summary

This report seeks Council's adoption of the 2021 Regional Fiscal Strategy, whose principles have guided the preparation of the 2021 Budget.

The report recommends that Council adopts the resolution shown as Attachment 2, requesting the Province to amend the *Development Charges Act* to ensure developments fairly contribute to the cost of the Yonge Subway Extension. The resolution also requests the Province to renew the growth-related cost supplement component for York Region's Annual Repayment Limit (ARL) under *Ontario Regulation 403/02*.

This report also recommends the early repayment of $18.7 million of the tax levy and user rate debt that is due to be refinanced in 2021.

Furthermore, the report seeks the adoption of the 2021 Long-Term Debt Management Plan that would allow the Region to access the growth-related cost supplement for its Annual Repayment Limit.

Finally, this report seeks Council's approval to transfer contributions previously made by YorkNet from the Region's reserves to its own reserves.

3. Background

Each year Council adopts an updated fiscal strategy

Each year Council adopts an updated fiscal strategy as part of its budget considerations. The last fiscal strategy that was adopted by Council can be found as item I.2 on the Committee of the Whole Agenda of December 12, 2019.

The fiscal strategy helps to achieve long-term financial sustainability through carefully managing the Region's capital plan, its reserves and debt. These elements are shown as Figure 1.

Figure 1
Elements of the Fiscal Strategy

Source: York Region Finance Department

The Region will be asked to make a significant financial contribution towards the cost of the Yonge Subway Extension

On April 10, 2019, the Province committed to building four subways for a total expected cost of $28.5 billion, including the Yonge Subway Extension (YSE). The YSE is expected to be in service by 2029-2030 and will be a vital piece of the infrastructure needed to achieve the planned population and employment growth of the Region.

On May 28, 2020, Council authorized the execution of a preliminary agreement with the Province to work towards delivering the YSE. While the formal contribution agreement has yet to be negotiated, staff estimate that the Region could be asked to contribute over $1 billion towards this project.

Although the Yonge Subway Extension is not reflected in the Region's current 10-year Capital Plan, the fiscal strategy also examines how its expected financial contribution towards this project could impact future levels of debt and reserves.

Changes to the *Development Charges Act* are needed to ensure that development that benefits from the YSE fairly contributes to its costs

In June 2020, the Chair and the Mayors of our largest three municipalities requested that the Province provide financial tools required to help ensure that growth that benefits from the subway pays its share of the costs. Among other things, this request sought changes to the *Development Charges Act* that would:

- **i.** Treat the YSE as a discrete service with no specified time limits on the planning horizon, and
- **ii.** Exempt the YSE from the rate-freezing provisions implemented recently under this Act

While the Province has not formally responded, Regional staff have been actively working with Provincial staff regarding these requested changes.

A further discussion on this matter is found later in this report.

A renewal of the growth-related cost supplement will be essential for financing additional major projects

The Annual Repayment Limit regulation, under the *Municipal Act, 2001*, limits the amount of debt and other financial obligations that a municipality can assume.

The ARL restricts the annual cost of servicing the anticipated long-term debt and financial obligations of a municipality to 25 per cent of its own source revenue. However, the provincial definition of "own source revenue" does not include development charges, which are an important revenue source for the Region.

In 2011, the Province recognized York Region as a high growth municipality with unique debt requirements and passed a York-specific regulation that would allow it to include a portion of its development charges as part of its own source revenue. This regulation expires at the end of 2021. While, the Region is projected to remain within its basic ARL limit under the proposed 10-year Capital Plan, the additional flexibility provided by the renewal of the growth-related cost supplement would be necessary to finance the YSE without limiting the ability of the Region to grow.

A more fulsome discussion of the growth-related cost supplement can be found on pages 2-3 of the 2021 Long-Term Debt Management Plan attached to this report.

4. Analysis

The overarching principles of the fiscal strategy are to achieve long-term financial sustainability and intergenerational equity

The fiscal strategy is based upon the principles of achieving long-term financial sustainability and intergenerational equity, which means that no generation is left worse off through the actions of another. These two principles guide decisions about when infrastructure will be built, how it is funded and the amount that can be financed.

The Region makes two types of infrastructure investments: those needed to facilitate growth, and those needed for asset rehabilitation and replacement.

Some assets must be built for growth to occur. Debt can be used to bridge the timing difference between when a growth-related asset is built and when it is eventually paid for through development charge collections, which can be years later. The principle of intergenerational equity requires that debt be kept to a sustainable level, such that its credit rating can be maintained.

The cadence and magnitude of projected future development charges collections will be key determinants of debt capacity. Spending too far ahead of growth could leave the Region with too much debt and an underutilized asset base that needs to be maintained, while too little spending could slow the rate of growth. Therefore, the monitoring of the pace of growth may require adjustments to the capital plan from time to time to ensure that it is aligned.

Infrastructure assets can also be used for many generations. In order to achieve equity over time, the goal for funding asset rehabilitation and replacement projects is to ensure each generation pays its fair share of the cost of using these assets. Intergenerational equity means that future generations will not need to borrow to maintain the roads and water systems and other infrastructure assets in a state of good repair. To ensure each generation pays their fair share, annual contributions to reserves have been calculated using a very long time horizon – 100 years. When the assets are relatively young, reserve contributions may exceed the draws and reserve balances will grow. Over time, reserve balances will decline as assets age and then need to be repaired or replaced.

Applying the principles of long-term financial sustainability and intergenerational equity to the Region’s infrastructure program requires the careful balancing of three separate streams of activities: managing the capital plan and using reserves and debt to ensure the delivery of projects at the appropriate time and at the lowest cost to taxpayers. Achieving this balance without taking on excessive financial risk requires continuous monitoring.

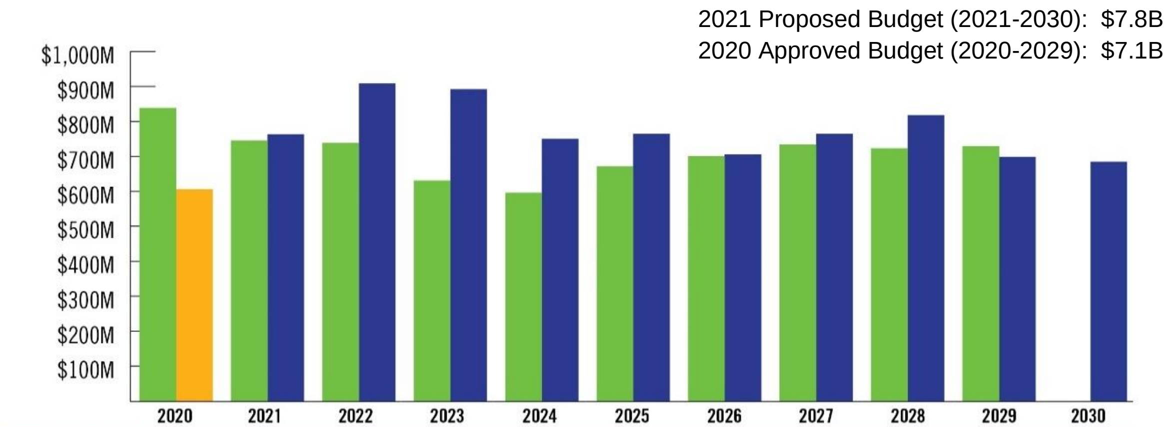
The remainder of this report discusses the elements of the fiscal strategy in more detail, as well as the Region’s credit ratings, requests to the Province, the Long-Term Debt Management Plan and the potential impact that the YSE could have on all these factors.

FIRST ELEMENT OF THE FISCAL STRATEGY – MANAGING THE CAPITAL PLAN

At $7.8 billion, the proposed 10-year Capital Plan is $642 million higher than last year, as shown in Figure 2. The capital plan includes approximately $4.6 billion for new growth-related infrastructure and approximately $3.2 billion for rehabilitation and replacement, which is detailed in Figure 3.

Figure 2

10-Year Capital Plan Comparison

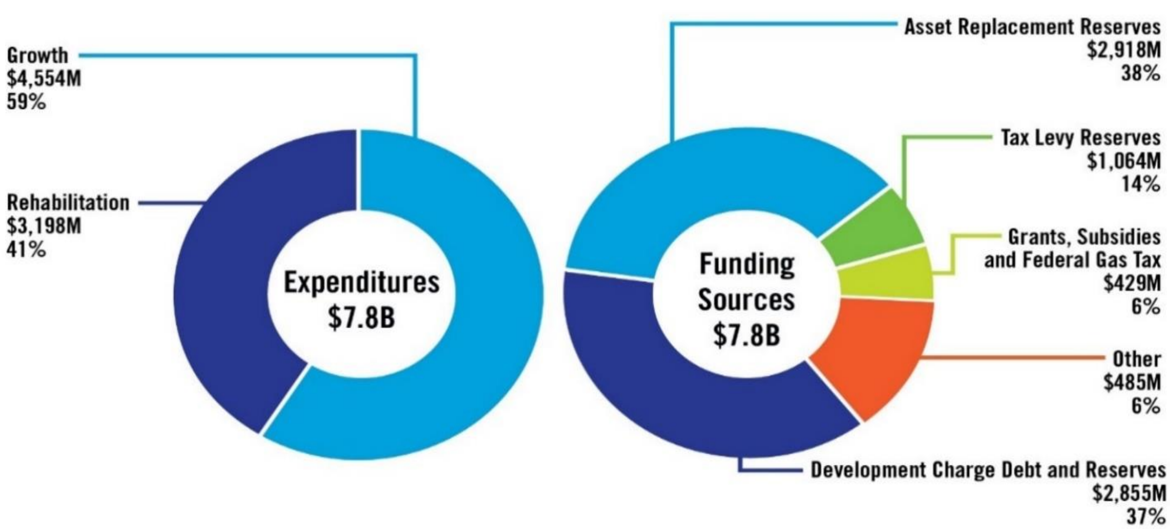


	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
2020 Budget	839	746	738	631	596	672	701	734	723	729	
2021 Budget		763	909	892	751	765	706	765	818	698	684
2020 Forecast	606										

Source: York Region Finance Department

Figure 3

Growth and Rehabilitation Expenditures and Funding Sources from 2021-2030



Source: York Region Finance Department

Recent amendments to the Growth Plan extend the planning horizon to 2051

Municipalities within the Greater Golden Horseshoe are required to conform to the targets set out by the provincial Growth Plan. Due to this legislative regime, there is a cascading effect that has financial implications for the Region (Figure 4). In August 2020, the Province amended its Growth Plan to extend its planning horizon from 2041 to 2051.

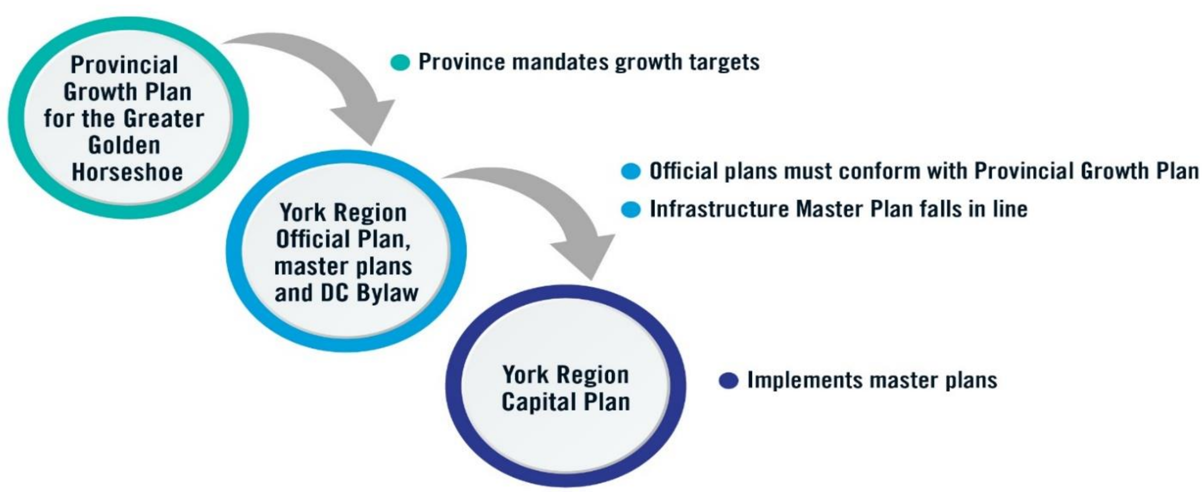
York Region's Official Plan must conform to the provincial Growth Plan, while its infrastructure master plans must also include what is needed to create complete communities that will meet the expectations of residents and Council. Master Plans are implemented through successive 10-year capital plans. If the population contemplated by the Growth Plan varies significantly from what is experienced in the near term, the timing of spending in the capital plan may need to be adjusted to reflect the expected rate of population growth or the municipality could face the risk of having an unmanageable level of debt as well as excess infrastructure capacity which could create operating budget pressures in excess of assessment growth.

Under the amended Growth Plan, the Region is mandated to plan to accommodate 2.02 million residents and 990 thousand jobs by 2051. This equates to an average annual population growth of about 26,100 residents over the 30-year forecast horizon. By comparison, from 2010 to 2020, the Region grew by approximately 16,500 residents per year.

Through the Municipal Comprehensive Review process, staff are working to ensure that infrastructure capacity and timing to meet the growth targets are fully considered and aligned. In addition, there will be opportunities to re-calibrate Regional plans to reflect observed growth through future Municipal Comprehensive Reviews, Master Plan updates, and the annual budget process.

Figure 4

How the Growth Plan informs the 10-year Capital Plan



Source: York Region Finance Department

The Region continues to make significant investments in growth-related capital

The Region continues to make significant investments in growth-related capital. As previously shown in Figure 3, the 10-year Capital Plan includes $4.6 billion of growth-related infrastructure, which is an increase of over $500 million (12 per cent) compared to last years' 10-year Capital Plan. The growth component accounts for approximately 59 per cent of planned expenditures.

Provincial legislation prohibits the entire cost of growth being paid for through the use of development charges. Approximately $2.9 billion of the $4.6 billion of growth-related spending is expected to be funded from development charges while the remaining $1.7 billion is expected to be mostly funded from tax levy, federal gas tax and grants from other levels of government.

Approved asset management plans have been incorporated into the Capital Plan

All departments have completed asset management plans that inform their long-term capital plans. Over the next 10 years, asset management spending is slightly higher than shown in last year's budget, mostly due to updated asset condition assessment information provided as part of our ongoing asset management efforts.

As was shown in Figure 3, most of the asset management spending, or $2.9 billion, will be funded from asset replacement reserves, while the remaining $300 million will be funded from other recoveries, grants and reserves.

SECOND ELEMENT OF THE FISCAL STRATEGY – RESERVE MANAGEMENT

Reserve management is an important element of the fiscal strategy. Reserves help fund the spending for capital assets as well as smooth tax levy and user rate requirements. They also provide financial flexibility in the event of unanticipated expenditures or drops in revenue, such as what could be experienced as a result of COVID-19. In addition, because reserves include both cash and cash equivalent assets, they also promote investor confidence and help to preserve the Region's credit ratings.

As of December 31, 2020, the Region's 60 reserves held approximately $3.2 billion which have been grouped into the six categories shown in Figure 5.

Figure 5
Estimated Reserves at December 31, 2020

Reserve Balance ($Millions)	Tax Levy	User Rates	Development Charges	Other	Total	2020 Target*
Asset Replacement Reserves	1,203	528			**1,732**	1,800
Growth Capital Reserves	371		276	86	**733**	710
Debt Reduction Reserve	242				**242**	At Target
Stabilization Reserves**	109	59		116	**283**	At Target
Other Corporate Reserves	95			1	**96**	At Target
Human Resources Reserves***	116				**116**	250
Total	**2,135**	**587**	**276**	**203**	**3,201**	
Share in Total	**67%**	**18%**	**9%**	**6%**	**100%**	

Source: York Region Finance Department
*These targets currently exclude subway cashflow needs (estimated at $1.3 billion)
**Other includes Pandemic Management Reserve which is expected to have a balance of $63 million
***Target represents contingent liability. Expected annual costs are included in approved budget figures (e.g., WSIB, LTD, health & dental)

As per Council policy, targets for the tax levy and user rate reserves have been established that would ensure funding for future capital expenditures will be available without the need to issue any new debt.

Asset Replacement Reserves will be used to keep $15 billion of today's assets in a state of good repair

The largest reserve category, at approximately $1.7 billion, will be used for future asset rehabilitation and replacement. Of this, approximately $1.2 billion will be for tax levy supported assets and $528 million will be for user rate supported assets. Taken together, the total reserve balance is just shy of their 2020 targeted amount.

Since some assets may be used by several generations of residents and businesses, reserve targets and their annual reserve contributions are typically calculated based on their needs over a very long-term horizon – 100 years. The contributions to these reserves are smoothed to not disproportionately affect future tax or user rates.

The estimated replacement value of the Region's assets now stands at over $15 billion, and the 10-year Capital Plan includes the addition of another $4.6 billion of new assets. Eventually, this infrastructure will need to be rehabilitated or replaced and the $1.7 billion currently set aside in the asset management reserves will need to grow significantly to fund this cost.

The draws from the tax levy asset replacement reserves used in the forecast are based on departmental submissions as part of their capital plans. Contributions to the reserves for 2021 and 2022 outlook period are based on what is shown in the proposed operating budget. However, because budgets and outlooks are only approved for the term of a council, assumptions must be made for the purpose of long-term reserve forecasting.

Forecasted tax-levy supported reserve balances assume that progress towards funding targets will be the result of contributions made at the same pace as annual tax-levy increases of approximately 3per cent plus assessment growth, which is in line with recent experience.

Council's commitment to the full cost recovery of water and wastewater costs guides the forecast for the user rate reserves. The current approved water rate study assumes 2.9per cent annual user-rate increases for 2022 and beyond. However, the water and wastewater reserve projections were amended on [April 2, 2020] and then on [December 10, 2020], to reflect Council's decisions not to increase user rates for 2020 and 2021.

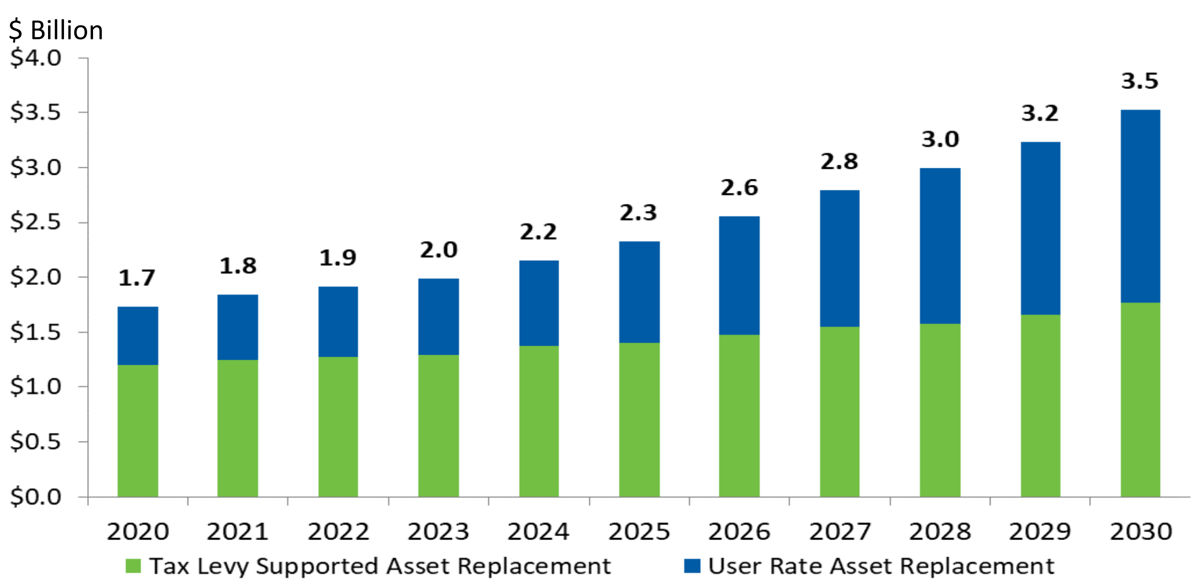
All reserves assumptions are reviewed annually, based on Council decisions, and will also be updated for the new rate study expected later this year.

Over the next ten years user rate reserves account for almost three-quarters of the projected increase in the capital asset replacement reserves

Figure 6 shows that the overall reserve balance for asset management is expected to increase from $1.7 billion in 2020, to nearly $3.5 billion by 2030. Approximately $1.3 billion of this increase is attributable to the user rate reserves while the remaining $500 million is attributable to the tax levy reserves.

Figure 6

Capital Asset Replacement Reserve Balances (2020-2030)



Note: Assumes annual increases to Asset Replacement reserves from 2022-2030 discussed above
Source: York Region Finance Department

Except where noted, most other reserves are projected to be fully funded over the next ten years

At approximately $733 million, the growth capital reserves represent the second largest category of reserves. These fund the growth-related capital component of the 10-year Capital Plan and are currently slightly above their target for 2020.

The Debt Reduction Reserve, with an approximate balance of $242 million, is currently on target to fund future capital projects that would have previously required the issuance of tax levy debt. The 2020 year-end balance of this reserve was at its target level. However, if it is needed to provide future tax levy funding for the YSE, there may be a requirement for a higher level of contributions to this reserve.

The stabilization reserves are available to pay for any unexpected expenditures or revenue shortfalls. The estimated balance of $283 million includes $109 million for the tax and fiscal stabilization reserves which are available to offset any unexpected tax levy pressures. The $59 million in the user rate stabilization reserve is to help mitigate against any user rate fluctuations arising from unforeseeable events.

Also included in the stabilization reserve category is the new Pandemic Management Reserve Fund, which Regional Council established on December 10, 2020. This reserve will help fund future tax levy expenditure or revenue shortfall that may arise due to COVID-19 and has an estimated year-end balance of $63 million. With the addition of the new Pandemic Management Reserve, the stabilization reserves are currently at their targeted levels.

Other corporate reserves include operating reserves for specific purposes, such as the Green Energy reserve and the Provincial Gas Tax reserve. These reserves are also at target.

The last reserve category is for future human resources liabilities, which are currently below their target. Targets for these reserves are based on liability valuations made from time to time by actuaries. In addition to the annual budgeted contribution to these reserves, the Surplus Management Policy has, in prior years, allocated a portion of the operating surplus to help close the gap. However, Council has temporarily suspended this Policy and directed that any operating surplus be contributed to the Pandemic Management Reserve.

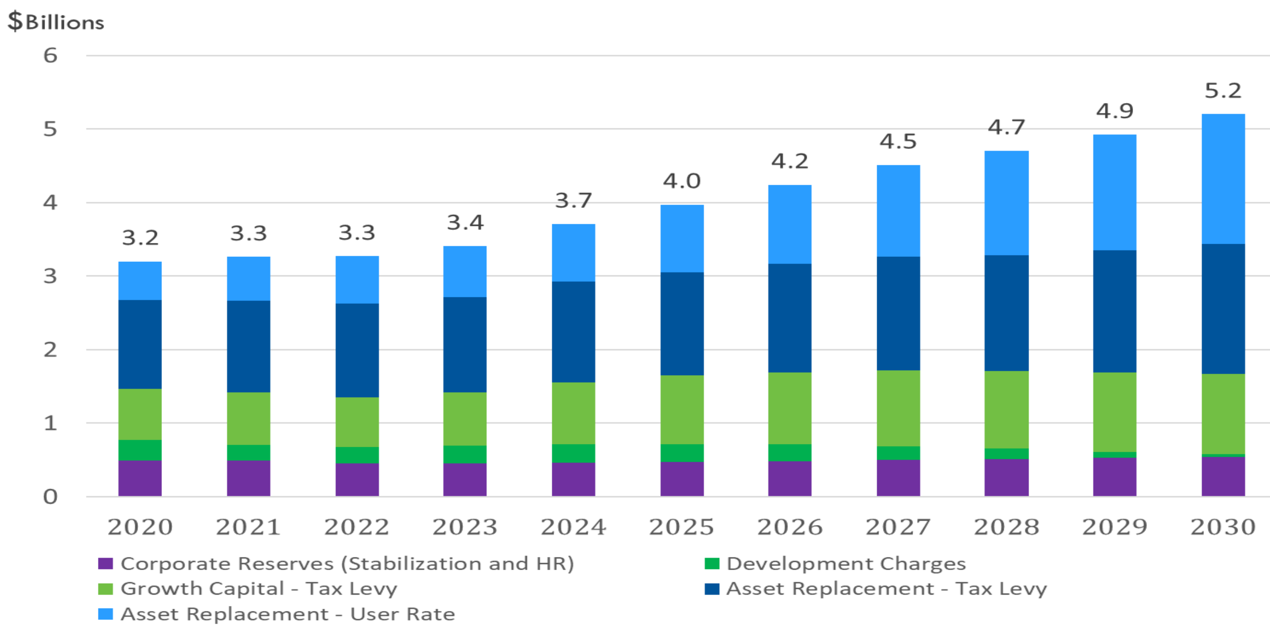
The figures and discussion above do not include the Sinking Fund Reserve, which is a non-discretionary reserve required by statute and can only be used to repay outstanding debt. As of December 31, 2020, the balance in the Sinking Fund Reserve was approximately $832 million.

Total reserves could grow to $5.2 billion by 2030

Figure 7 shows that total reserves could grow to approximately $5.2 billion by 2030. This forecast does not assume the use of any of these reserves for the funding of the Yonge Subway Extension. A further discussion regarding the impact of funding the subway is found later in this report.

Figure 7

Total Reserves (2020 – 2030)



Source: York Region Finance Department

THIRD ELEMENT OF FISCAL STRATEGY – DEBT MANAGEMENT

Debt is a tool that the Region uses in order to provide capital infrastructure needed in advance of receiving the funding for it. Debt is not a source of funding and must be repaid over time.

The use of debt is governed by both provincial legislation as well as the Capital Financing and Debt Policy approved by Council.

Since 2016, Council's policy has been to avoid issuing any new tax levy or user-rate supported debt. At the end of 2020, approximately 93 per cent of the net debt outstanding was issued for growth-related capital projects and will be funded from future development charge collections, as shown in Figure 8 below.

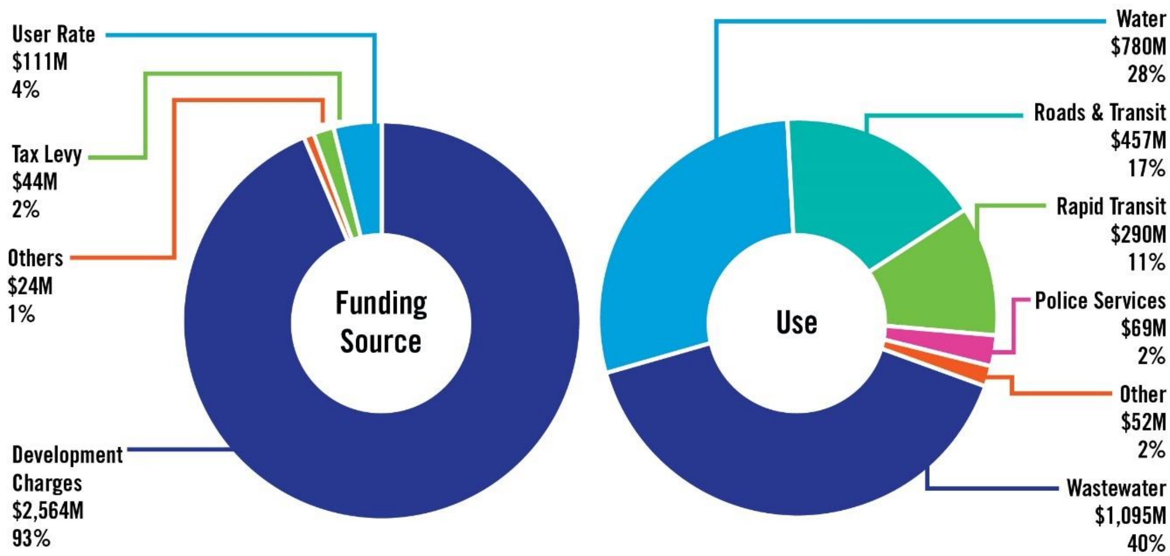
Carefully managing new debt requirements is the best way to mitigate the risk that growth could be slower than needed to service outstanding debt. It also helps to preserve fiscal flexibility and ensures that the Region continues to have access to the financial capital markets at an affordable rate of interest.

Because of the size of its borrowing programs, almost all the debt that is issued by the Region is defined as term debt. Under provincial regulations, term debt requires that the Region put an amount each year into a sinking fund that will be used to fully pay back the principal amount upon maturity of the debt.

Figure 8

Outstanding Net Debt – York Region as at December 31, 2020

$2.7 Billion



Note: Outstanding net debt is an estimate and subject to change as part of year-end adjustments.
Source: York Region Finance Department

For reporting purposes, it is the generally accepted practice to show the outstanding debt after deducting the amount held in the sinking fund. Net debt is the difference between the gross debt outstanding and the total contributions and accumulated interest in the sinking fund.

A further discussion on the risks associated with debt, as well as the mitigation strategies used by the Region, is discussed in Section 3 of the 2021 Long-Term Debt Management Plan that is attached to this report.

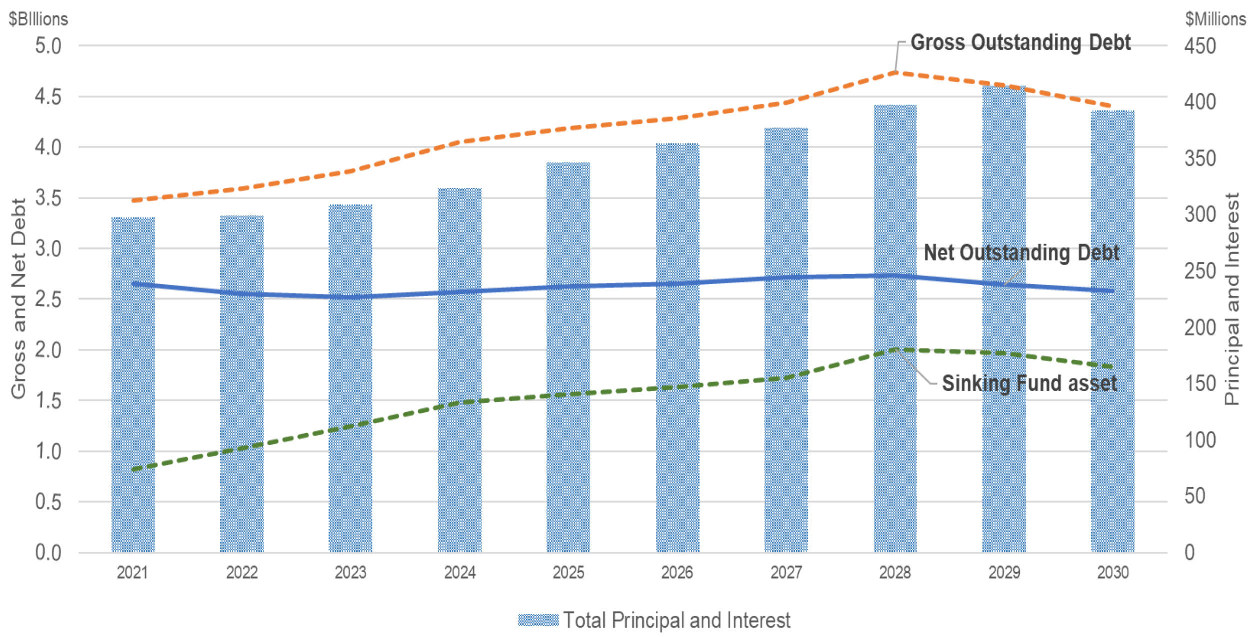
Principal and interest payments are based on the gross debt outstanding

The forecasted principal and interest payments over the next ten years are shown as blue bars in Figure 9 below. These payments are based on the estimated amount of gross debt outstanding (shown as the orange dashed line), which includes new growth-related debt required to implement the proposed 10-year Capital Plan. Net debt, which was discussed earlier, is shown below as the blue line.

Figure 9

2021 Proposed Budget Debt Forecast

Gross vs. Net Debt and Principal and Interest



Source: York Region Finance Department

DC collections are expected to return to pre-COVID-19 levels by 2022

Development charges are the main source of funding for the growth-related infrastructure built by the Region as well as the sole source of funding for the payment of principal and interest on outstanding and new debt issued for that purpose.

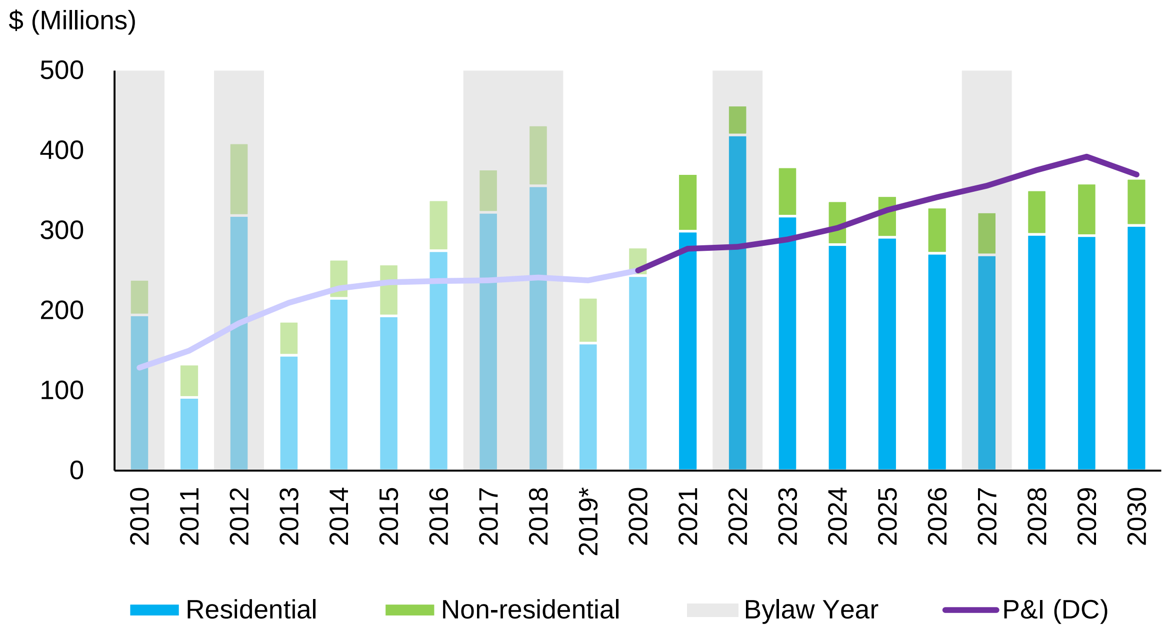
Figure 10 shows the forecasted development charge collections as well as anticipated principal and interest payments for the proposed 10-year Capital Plan.

Actual development charges collections for 2020 were below forecast due in part to the impact of COVID-19 on development activity and the overall economy.

The ten-year development charges collections forecast for the 2021 Budget anticipates that collections will return to their pre-COVID-19 levels by 2022 resulting in collections of about $3.6 billion from 2021 to 2030.

Figure 10

Historic and Forecasted Development Charge Collections and P&I



**Bill 108, More Homes, More Choice Act, 2019* was introduced

Source: York Region Finance Department

Development charge collections are forecast to be, on average, $362 million per year, while average principal and interest payments during this period are expected to be $331 million per year, on average. If collections were to be even 10 per cent less, on average, during this period, this could require up to $300 million of capital projects needing to be deferred to future years to maintain the current debt profile and credit rating. It is anticipated that there will continue to be significant year-over-year fluctuations with collections. Some years are forecast to fall short of the principal and interest payments needed for development charge related debt and will therefore require close monitoring.

A detailed discussion on the long-term development charges collections forecast for the Region can be found on pages 10-12 of the 2021 Long-Term Debt Management Plan that is attached to this report.

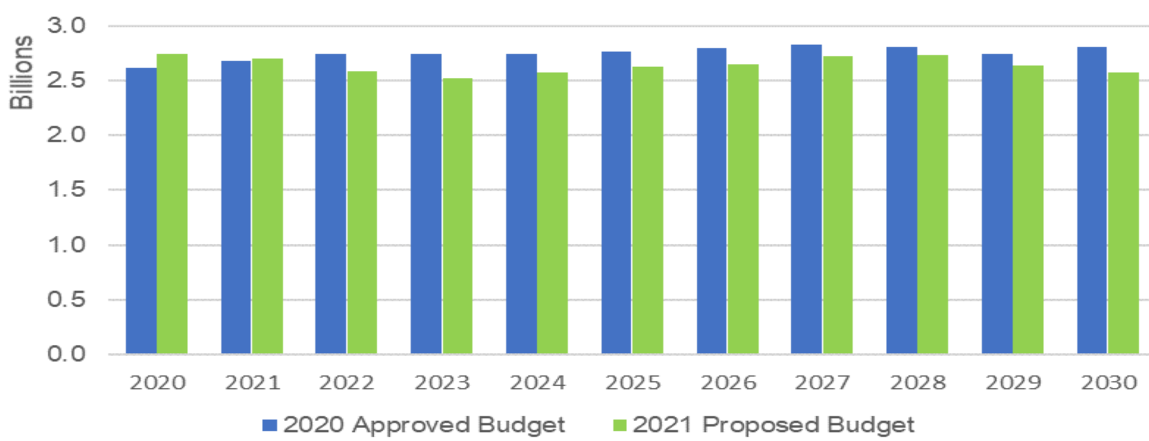
Projected debt levels are related to financing infrastructure needed for future growth

The 10-year Capital Plan includes approximately $4.6 billion for new growth-related infrastructure, for which approximately $2.3 billion of new debt will be needed (Figure 11). During the ten years from 2021 to 2030, the Region will also be required to pay approximately $3.5 billion in principal and interest to service its existing and future debt.

While the growth component of the 10-year Capital Plan increased by approximately $500 million, the forecasted net debt profile has improved compared to last years projection, due to the improved forecast of development charges collections this year as well as a projected lower interest rate environment.

Development charges collections are now forecasted to be $319 million higher than what was anticipated in the 2020 budget over the 2021-2030 period. The improvement in the collections forecast is mainly due to the positive impact of Bill 138, which reversed a previous proposal to allow non-residential development to delay and phase their payments. The improvement in debt was also impacted by the assumption of lower interest rates which are now expected to continue over the mid-term.

Figure 11
Outstanding Net Debt Projection by Year



Source: York Region Finance Department

The Region also needs to refinance a portion of maturing debt as part of its 2021 borrowing program

In 2011, York Region issued $450 million of 10-year debentures which will mature in 2021. However, some of the projects that were financed with those debentures required a debt amortization period of twenty years. Like a mortgage, there will still be an amount owing for those projects when the debenture matures. Figure 12 details the $270 million from this debenture that would have needed to be either refinanced or repaid in 2021.

In the Fall of 2020, the Region issued a debenture that included the early re-financing of $90 million of the Development Charge funded debt maturing on June 30, 2021. The purpose of the early refinancing was to reduce some of the market risk associated with the large re-financing required for 2021, as well as to lock in savings available from the historically low rates available at that time.

Figure 12

2021 Refinancing Requirements

Funding Source		Refinancing Required ($Millions)
Development Charges		249.2
Tax Levy		8.7
Provincial Subsidy		2.2
User Rate		
Wastewater	9.3	
Water	0.7	
		9.9
Total (before early re-financing)		270.0
Early re-financing issued in 2020		90.0
Total refinancing for 2021		180.0

Source: York Region Finance Department

In accordance with Council policy, it is recommended that $18,657,698 of tax levy and user rate debt coming due in 2021 be repaid from the following reserves:

1. Tax levy-funded Debt Reduction Reserve ($8,714,376);
2. User rate-funded Capital Asset Replacement Reserve - Water ($667,230), and
3. User rate-funded Capital Asset Replacement Reserve - Wastewater ($9,276,092).

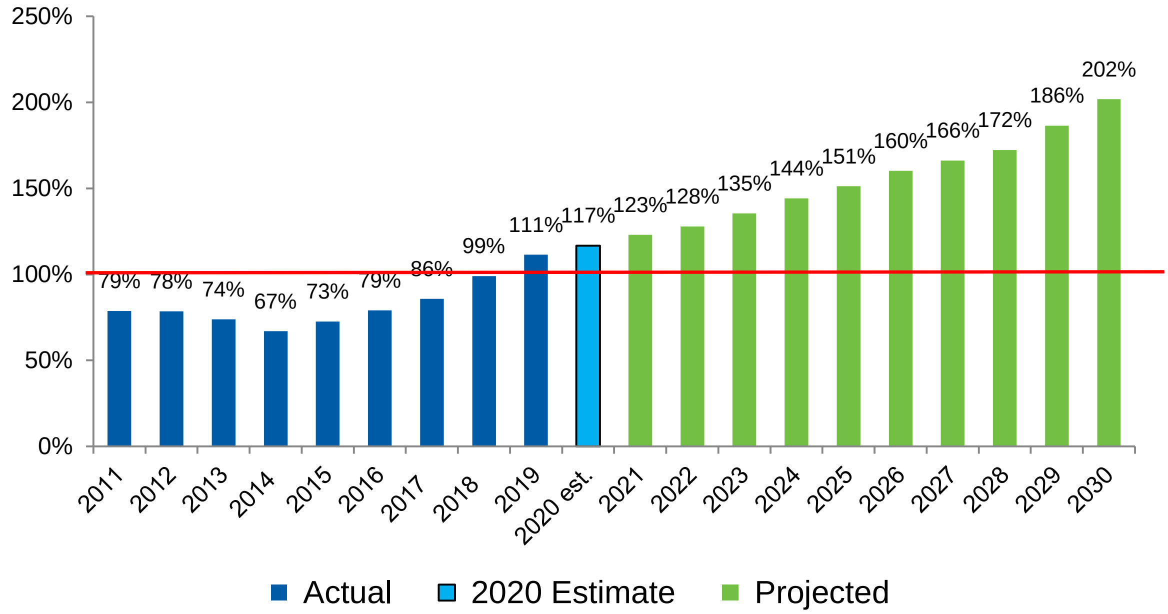
If approved, internal reserves would be used to reduce the amount of debt to be refinanced as part of the Region's 2021 borrowing program from $180 million to $161.3 million.

York Region has become a "net investor"

Figure 13 illustrates that since 2019, York Region has held more in reserves than it has in outstanding net debt. A reserve to net debt ratio greater than 100 per cent indicates that the Region is a net "investor" while a ratio of less than 100 indicates that it would be a net "borrower". The respective levels of debt and reserves are key considerations for rating agencies when evaluating the Region's credit worthiness. York's net investor status has been favorably looked upon by both rating agencies and investors.

With projected debt needed to implement the 10-year Capital Plan and the forecasted contributions to reserves, this ratio could reach 202per cent by 2030.

Figure 13
Reserve to Net Debt Ratios



Source: York Region Finance Department

YONGE SUBWAY EXTENSION

Financing York Region's contribution to the Yonge Subway Extension will require careful consideration

A preliminary YSE agreement was signed on May 28, 2020 in which the Region agreed to contribute its pro rata share of the municipal contribution towards the total capital construction cost of the project.

The project has been estimated to cost approximately $5.6 billion and based on preliminary discussions with the Province, staff anticipate that the Region could be asked to contribute over $1 billion towards it.

Staff have estimated the possible financial impact to the Region based on early-stage information. Revised forecasts for development charge collections that incorporate the subway (see later discussion), tax levy funded contributions for the non-growth portion, and construction timing that assumes completion in 2030, have been used for the projections shown below.

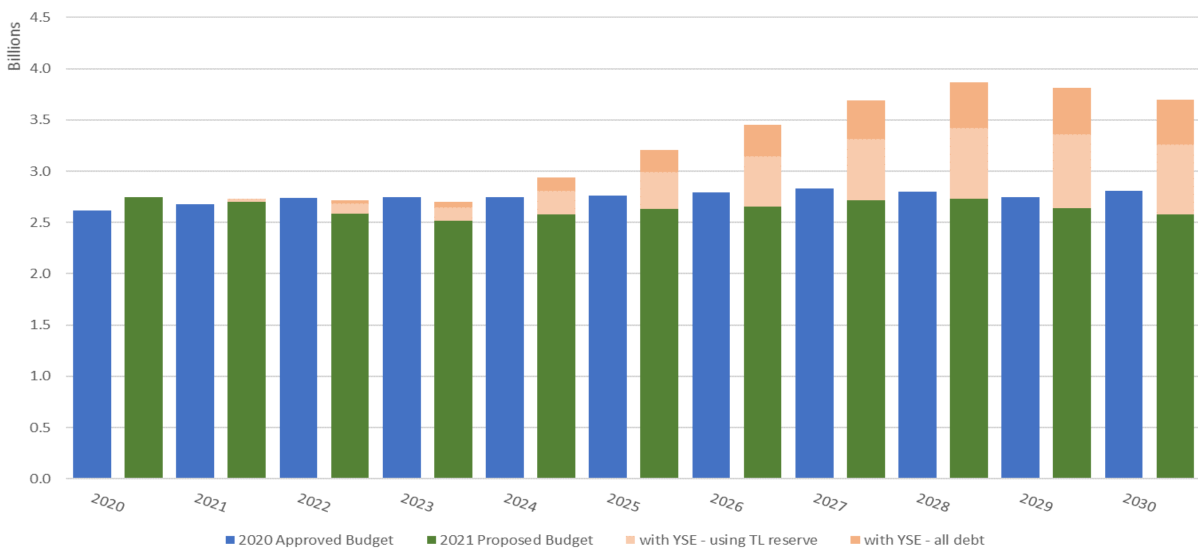
Staff have modeled two scenarios that show net outstanding debt increasing from $2.7 billion at the end of 2020 and peaking between $3.4 billion and $3.9 billion over the next 10 years as shown in in Figure 14. Both scenarios assume that tax-levy funded contributions to reserves will continue to increase at a rate of 3per cent per year plus assessment growth over the next ten years. Also, all the reserve draws assume that the timing of the payments for the YSE will be the same as the Region experienced with the Toronto-York Spadina Subway Extension.

The first scenario assumes that debt would only be issued for the growth-related portion of the Region's contribution and the remainder would be funded from tax levy reserves. Under this scenario, peak net debt would be approximately $3.4 billion and occur in 2028, which is about $500 million higher than the previous peak net debt level of $2.9 billion in 2017.

The second scenario assumes that the Region would finance its full contribution to the subway. This could allow the Region to smooth out the associated tax levy pressures over a longer period of time. However, the peak debt under this scenario, which would also occur in 2028, would be about $1 billion higher than the 2017 peak net debt.

Figure 14

Potential Net Debt Outstanding by Year including YSE

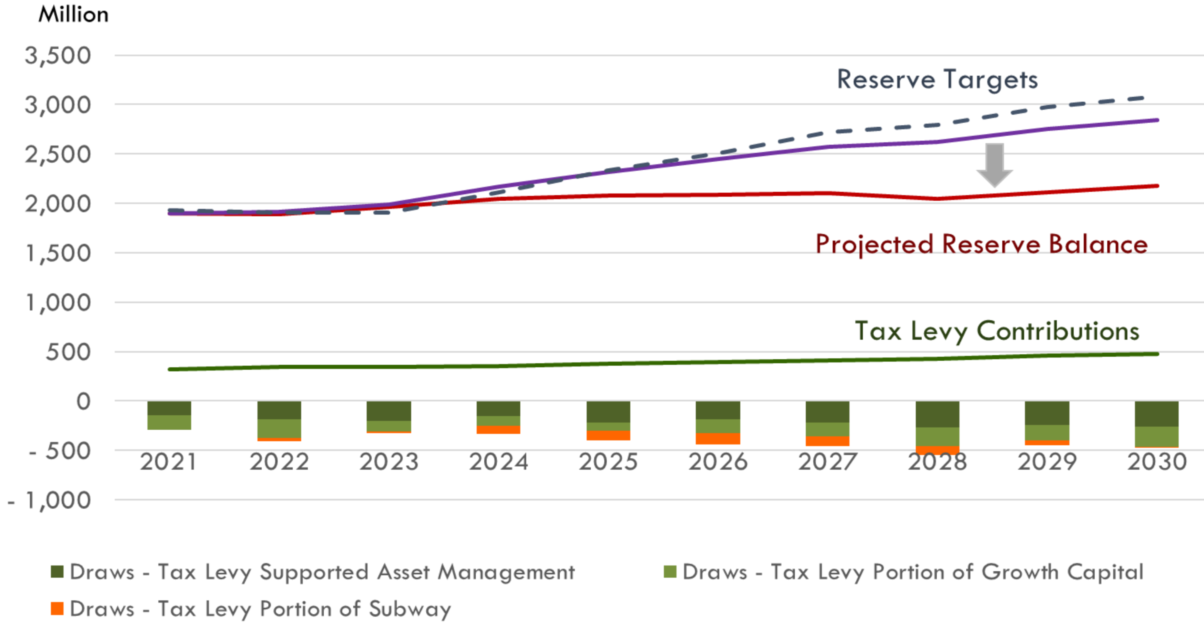


Source: York Region Finance Department

If tax levy reserves are used for the Yonge Subway Extension, projections indicate they could be up to 30per cent below their target by 2030

Figure 15 shows the tax levy supported reserves used to fund future capital projects. Over the next ten years, projected contributions are expected to average around $391 million and draws would average around $412 million if they are used to fund the non-growth component of the YSE. While the Region is on target today for its tax levy capital reserves, these reserves would start to fall below target once the construction on the subway begins, unless contributions from the tax-levy also increase over that time period.

Figure 15
Tax Levy Reserves for Capital (2020-2030)



Source: York Region Finance Department

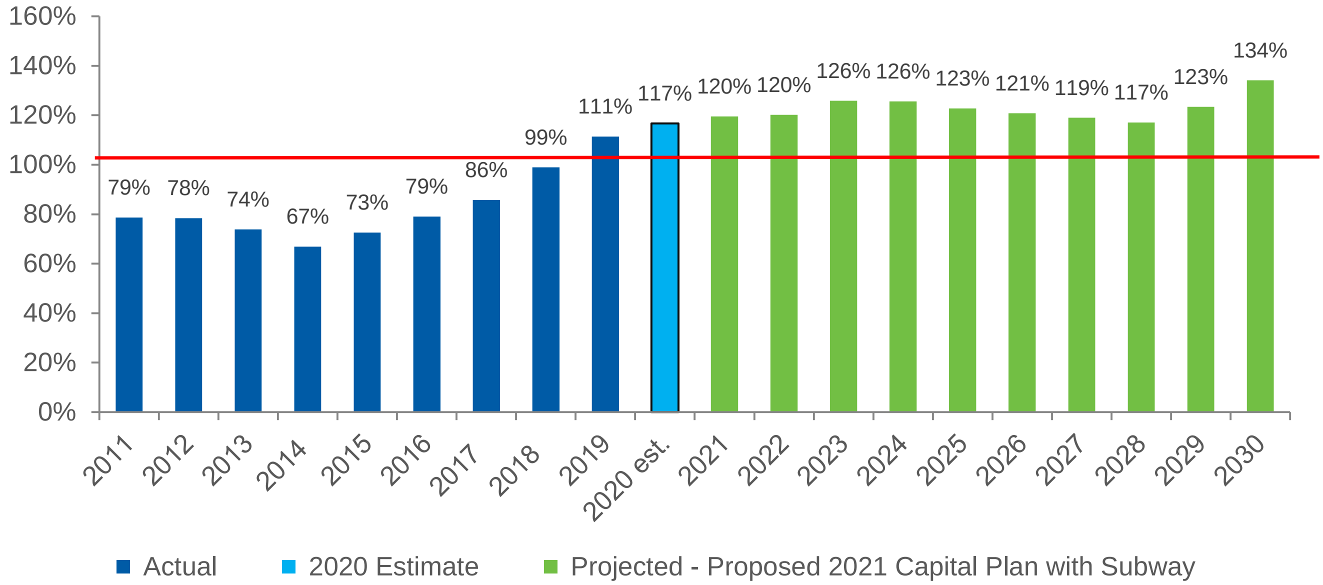
Without increasing contributions, the continued spending on growth capital, combined with the projected costs of the Yonge Subway Extension, would crowd out available fiscal room currently planned for asset management contributions. For tax levy assets, the gap between planned contributions and those needed to maintain the principle of intergenerational equity would widen over the next 20-years, with reserve balances that could be 30per cent below the target by 2030.

York Region would still be a net investor, but to a much lesser extent

Figure 16 shows the projected impact on the reserves to net debt ratio of using reserves to fund the non-growth component of the Yonge Subway Extension. When the impact of the cost of the YSE included in the values, the reserves to net debt ratio could drop a third, to 134per cent by 2030.

Figure 16

Reserves to Net Debt Ratios including YSE contribution from reserves



Source: York Region Finance Department

YORK REGION CREDIT RATING

Credit rating agencies have re-affirmed their respective ratings for York Region

In 2020, both S&P Global Ratings (S&P) and Moody's Investors Service (Moody's) re-affirmed their respective credit ratings for the debt issued by the Regional Municipality of York (Moody's – Aaa/ S&P – AA+ with positive outlook). This was supported by:

- A high level of cash and investments
- Prudent and far-sighted fiscal management
- A track record of positive operating outcomes
- Its diversified and expanding economy
- Considerable budgetary flexibility

This was the second consecutive year of a positive outlook by S&P Global Ratings. It reflected the possibility that, despite the pandemic, York's rating could return to triple A should economic growth continue to support a larger assessment base and should growth-related capital revenue continue to support the Region's evolving capital program.

Both Moody's and S&P remain concerned with the Region's high level of debt

Both rating agencies have expressed concern about the Region's high debt burden, especially relative to other rated Canadian municipalities.

In particular, Moody's and S&P identified three factors that could lead to a future downgrade:

- a sustained increase in the debt burden
- a material decline in liquidity
- if management's commitment to fiscal sustainability weakened in the face of slower economic growth

Rating agencies expect that the risks related to the COVID-19 pandemic will be mitigated by the Region's strong management and budgetary flexibility

The Region's exposure to the COVID-19 pandemic was viewed by both credit rating agencies as a risk that could result in fiscal pressures, stemming from increased demand for government services and infrastructure spending, which in turn could elevate the debt burden.

However, the opinion of both rating agencies is that York's strong financial management, stable property tax base and budgetary flexibility in part attributable to prudent saving in operating reserves will help cushion the impact and help guide it through this difficult economic time to maintain financial sustainability.

The Yonge Subway Extension has not been factored into the credit ratings

Credit rating agencies base their opinions on known strengths and risks over the near to mid term. As the YSE is not currently a part of the Region's capital plan, they have not factored in the financial impact of this into their analysis.

As shown in Figure 16 above, when considering the contributions expected for the YSE, the Region's reserves-to-debt value still maintains a net investor status. However, funding the subway still remains a risk.

REQUESTS TO THE PROVINCE

Changes to the *Development Charges Act* are required in order for the Region to continue on its path towards financial sustainability while funding its share of the Yonge Subway Extension

Development charges are expected to fund up to 80per cent of the cost of York's contribution to the Yonge Subway Extension. As discussed earlier in this report and consistent with other growth projects, the Region will need to issue debt to bridge from the time that it pays its share of the project to the time it receives the development charges needed to fund it.

The speed that the Region can recover its costs depends on how the YSE is treated under the *Development Charges Act.* Any methodology that would allow the Region to collect development charges for the YSE faster would lead to additional funding capacity and reduce the amount of future debt required.

Currently, the Yonge Subway Extension would be considered under the "transit" category, meaning its planning horizon for each bylaw is limited to 10 years. Legislative changes are required to treat the subway as a discrete service not subject to a 10-year horizon limit –

something done previously for the Toronto-York Spadina Subway Extension. Treating the Yonge Subway Extension as a discrete service, with no specific limit on the planning horizon, could improve cost recovery and lower debt pressures.

Recent changes to the *Development Charges Act* mean that developers can now lock in their development charge rates prior to the subway being added to the Region's bylaw. This change creates a significant disconnect between those who benefit from the subway and those who pay for it. Development charge eligible costs not recovered from developments that have locked in the pre-subway rates would be pushed onto and paid for by future developments in the form of higher development charge rates. Either repealing the freezing provisions in the *Development Charges Act*, or exempting the Yonge Subway Extension from them, could help correct this disconnect.

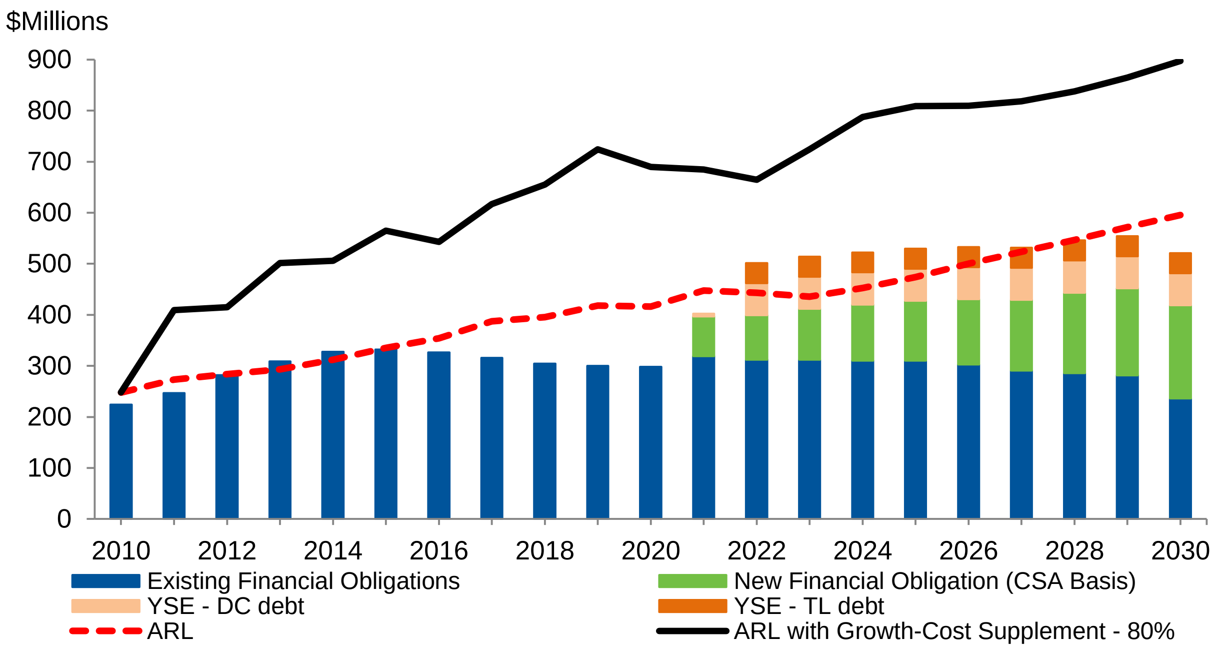
Removal of the freezing provisions in the *Development Charges Act* for the YSE would also result in improved cost recovery and ensure that more of the development that will benefit from the YSE will contribute to its fair share of costs.

The renewal of the ARL will be critical to finance York Region's contribution to the YSE and other major projects

Staff have been in discussions with the Province regarding the need to renew the growth-related cost supplement component of its ARL to allow York Region the ability to finance the YSE (Figure 17). This regulation will expire on December 31, 2021 and greater certainty in this matter is needed for staff to do long-term financial planning.

Figure 17

Annual Repayment Limit with YSE



Source: York Region Finance Department

Renewal of the ARL growth-related cost regulation would ensure that the Region would be able to finance its 10-year Capital Plan as well as the YSE. In the event the regulation is not renewed, the Region may need to defer some of the capital projects required to strive toward the provincial Growth Plan target.

2021 LONG-TERM DEBT MANAGEMENT PLAN

The 2021 Long-Term Debt Management Plan needs to be affirmed to access the growth-related borrowing capacity

In 2011, the Province recognized that York Region is a high growth municipality with unique debt requirements and provided a York-specific regulation that allows it to borrow a higher amount based on its development charges collections. In 2013 and 2014, the Region could have breached the annual repayment limit in the absence of the growth-related cost supplement.

To qualify for this additional growth-related borrowing capacity, Council is required to adopt a plan for the management of its long-term debt and financial obligations on an annual basis. This plan is provided as Attachment 1 to this report.

PROPOSED CHANGE TO REGIONAL RESERVE FUNDS

Council authorize the transfer of YorkNet's contributions from Region's reserves to its own reserves

In May 2020, YorkNet's board approved its own reserve policy and is working with staff to set-up separate reserve accounts in the financial reporting system expected by the end of the first quarter in 2021.

Between 2019 and 2020, YorkNet contributed $668,183 to the Region's General Capital Reserve and $321,988 to the Region's Tax Stabilization Reserve. In addition, the 2021 Budget includes a proposed contribution of $535,387 to the General Capital Reserve and $137,988 to the Tax Stabilization Reserve for 2021.

Council authority is now required to transfer the reserve contributions that were temporarily held in the Region's reserves to YorkNet's own reserves. It is proposed that up to $1,203,570 of contributions from the General Capital Reserve and up to $459,976 contributions from the Tax Stabilization Reserve will be transferred to YorkNet's Capital Asset Replacement Reserve and Stabilization Reserve respectively.

5. Financial

As part of the annual budget process, the Region assesses its finances, the general state of the economy and its infrastructure plan to formulate an annual updated fiscal strategy. Based on a continued commitment to the approved budget outlook and the fiscal strategy, the Region was able to ensure long-term financial sustainability by maintaining high levels of liquidity, saving adequate reserves for future asset management needs and reducing the need for new debt.

Adoption of this year's fiscal strategy is expected to result in the following financial impacts over the next ten years:

- Net outstanding debt will peak at $2.7 billion
- New debt that will be issued $2.3 billion
- Debt repaid $2.5 billion
- Reserves will increase by $2.0 billion

The funding of the Region's contributions towards the construction of the YSE project has not been included in the 10-year Capital Plan and so are not reflected in the numbers above.

6. Local Impact

Local municipalities will benefit from the fiscal strategy as it supports the Region's credit rating. Since local municipalities must issue all debenture debt and repay debt financing costs through the Region, a good credit rating helps to ensure that both the Region and local municipalities obtain the lowest possible cost of financing.

7. Conclusion

The fiscal strategy has resulted in careful management of the capital plan, an increase in reserves and reduced reliance on debt, all intended to help the Region achieve financial sustainability.

The fiscal strategy is updated annually and evolves as economic circumstances change and as more rigorous analysis is developed.

For more information on this report, please contact Edward Hankins, Director, Treasury Office and Deputy Treasurer at 1-877-464-9675 ext. 71644. Accessible formats or communication supports are available upon request.

Laura Mirabella

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Chief Administrative Officer

March 4, 2021
Attachments 2
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