The Regional Municipality of York

Committee of the Whole
Finance and Administration
February 9, 2023

Report of the Commissioner of Finance

2023 Regional Fiscal Strategy

1. Recommendations

1. Council adopt the 2023 Fiscal Strategy outlined in this report

2. Council endorse the 2023 Long-Term Debt Management Plan, shown as Attachment 1 to this report

3. Council authorize the establishment of the following reserve funds, as shown in Attachment 2, the Reserve and Reserve Fund Policy:

    a. The Tax Levy Development Reserve Fund, to fund the tax levy portion of development charge related phase-ins, discounts, and exemptions, such as those required by Bill 23, More Homes Built Faster Act, 2022

    b. The Rate Supported Development Reserve Fund, to fund the user rate portion of development charge related phase-ins, discounts, and exemptions, such as those required as a result of Bill 23, More Homes Built Faster Act, 2022

4. Council authorize transfers between the following reserve funds:

    a. $40.3 million between the various tax levy capital reserve funds outlined in Table 1 to align with the needs identified in the 2023 10-year Capital Plan

    b. $29.8 million from various tax levy and user rate reserves to development charge reserves to fund the cost of discretionary development charges exemptions under the 2017 Development Charges Bylaw, which was in place until June 16, 2022, as outlined in Table 2

5. Council approve technical amendments to the following policies, shown as Attachment 3:

    a. The Letter of Credit Policy to explicitly accept electronic Letters of Credit and to align the roles and responsibilities with the current organizational structure

    b. The Development Charges Interest Policy to revise the interest rate charged to be the average of the five largest Canadian bank's prime rates, plus 1%, which reflects the rules under the *Development Charges Act, 1997*, as amended.

6. Council direct staff to report back, as part of the Fiscal Sustainability Update Report in June 2023, on the fiscal impact of Bill 23, More Homes Built Faster Act, 2022, on future development charge collections and the recommended mechanism for funding any shortfalls

7. Council authorize the Regional Solicitor to prepare and/or amend the necessary bylaws

2. Summary

This report seeks Council's adoption of the updated fiscal strategy, whose principles were used to guide the preparation of the 2023-2026 Regional Budget.

It also seeks the affirmation of the 2023 Long-Term Debt Management Plan to allow the Region to continue accessing a growth-related cost supplement for its Annual Repayment Limit (ARL).

The report highlights the need for additional 1% incremental annual tax levy increases in 2023 and 2024 to fund the tax levy portion of the Yonge North Subway Extension (YNSE) as well as further 1% incremental increases for 2025 and 2026 to help fund the cost of additional infrastructure needs identified in the Region's master plans. The authority to levy these amounts has been included in the 2023 Budget as tabled and in the 2023 to 2027 Strategic Plan.

The report also recommends the amendment of several Council policies and reserve bylaws, as well as seeks approval to transfer funds between various reserves and reserve funds.

Finally, the report provides a high-level overview of the fiscal challenges resulting from Bill 23, More Homes Built Faster Act, 2022, and recommends that a more fulsome analysis and funding recommendations be included in the Fiscal Sustainability Update report to Council in June 2023.

Key Points:

- The 2023 fiscal strategy builds on achievements from successive fiscal strategies and continues to target long-term financial sustainability through the careful management of the capital plan, reserves and debt
- The continuation of one per cent incremental infrastructure-related tax levy increases, in addition to any operating increases, for each of 2023 and 2024 will be needed to help fund the Region's portion of the Yonge North Subway Extension (YNSE)
- The impact of higher inflation and interest rates will impact both the operating and capital programs
- Further one per cent incremental infrastructure-related tax levy increases for each of 2025 and 2026, in addition to any operating increases, will be needed to help fund the capital needs identified in the Region's master plans

- Bill 23 the *More Homes Built Faster Act*, will reduce development charge collections and has the potential to require additional tax levy and user rate increases to fund the shortfall
- In 2022, both S&P Global Ratings and Moody's Investors Service re-affirmed the Region's credit ratings at their highest levels, AAA and Aaa, respectively, owing to Council's commitment to prudent financial management

3. Background

THE EVOLUTION OF THE FISCAL STRATEGY

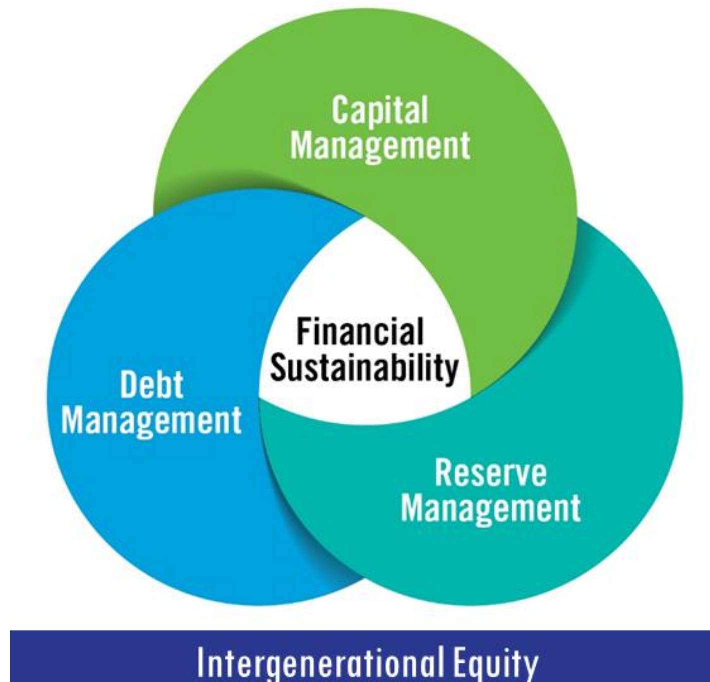
Council has adopted an updated fiscal strategy each year since 2014

As part of the 2014 Budget, Council adopted its first fiscal strategy, which has been updated annually as part of the budget process. The last fiscal strategy was adopted by Council on December 16, 2021, which can be found as item I.2 of the Committee of the Whole Agenda.

The fiscal strategy strives to achieve long-term financial sustainability while maintaining a balance between the current and future needs of the Region. This has been done through the prudent management of the capital plan, reserves and debt. These elements, as shown in Figure 1, work cohesively to achieve long-term financial sustainability.

Figure 1

Elements of the Fiscal Strategy



Source: York Region Finance Department

The Region's fiscal strategy is guided by the following four key principles endorsed by Council

Through the direction from Council and annual review of the fiscal strategy, the Region has been able to achieve a strong financial position. The fiscal strategy is guided by the following key principles:

- Keeping growth affordable and the existing infrastructure in a state of good repair
- Maintaining a "AAA" credit rating
- Having the fiscal flexibility to respond to the evolving needs and economic changes
- Treating current and future tax and rate payers fairly by striving for intergenerational equity

Keeping growth affordable means that the Region must prudently manage its growth spending, aligning it with anticipated development charge revenue, to ensure its strong financial position is maintained while enabling the creation of complete communities. At the same time, appropriate funding is dedicated to maintain existing infrastructure in a state of good repair.

Council's commitment to fiscal prudence has been recognized by the credit rating agencies. In 2022 both S&P Global Ratings (S&P) and Moody's Investors Service (Moody's) rated the Region's debt Triple A, the highest grade possible.

Having the fiscal flexibility to respond to evolving needs and economic changes is supported by Council's dedicated approach to carefully managing spending and building up reserves.

Treating current and future tax and rate payers fairly means that no generation is left worse off through the actions of another. This is particularly important when setting the capital plan and provisioning for the replacement and rehabilitation of capital assets, some of which have very long useful lives and significant costs. Although each successive fiscal strategy has worked towards achieving a greater intergenerational balance, the Region is not yet on target. Contributions to the tax levy-related asset replacement reserves are below the levels required to meet the needs of the Region's current and growing asset base over the long-term and projected contributions currently require future generations to fund more than their share.

Successive fiscal strategies have strengthened the Region's financial position

Prior to the 2014 fiscal strategy, the Region's outstanding debt was expected to exceed $5.0 billion by 2020. However, because of the actions that were taken by Council through past fiscal strategies, total outstanding net debt peaked at $2.9 billion in 2017 and is estimated to drop to $2.3 billion by the end of 2022.

Owing to the dedication of Council to meet the goals of the fiscal strategy, the Region is expected to have over $4.3 billion in over 60 reserves and reserve funds, making it a net

investor. The Region's reserves are held primarily for asset rehabilitation and replacement, corporate contingency and to fund the non-development charge portion of growth.

Higher reserve balances and lower debt levels have been the key contributors to the Region's superior credit rating.

Aligning infrastructure investment with growth will be the key to fiscal sustainability

The Growth Plan for the Greater Golden Horseshoe sets out population and employment targets for municipalities. Municipalities develop official plans that adhere to provincial requirements and infrastructure master plans that forecast the capital needs to support the planned level of growth.

Infrastructure investments often must occur in advance of when growth occurs and when development charges are collected. Debt is used to bridge the timing between infrastructure expenditure and revenue collection. Aligning and phasing infrastructure delivery is key to mitigating the financial risks associated with planning for growth and paying for the required infrastructure.

At the Region, financial plans such as the Development Charges Background Study and Bylaw, Asset Management Plan, fiscal strategy and the Budget provide the financial guidance to invest in the required growth-related infrastructure while remaining fiscally sustainable.

Between now and 2051, there will be multiple updates to these infrastructure and financial plans that will provide opportunities to either confirm, or if necessary, adjust forecasts and the timing of infrastructure delivery to reflect updated growth projections for the Region.

MAJOR NEW INFRASTRUCTURE PROJECTS WILL REQUIRE ADDITIONAL FUNDING

A continuation of the 1% annual increment to the Rapid Transit / Infrastructure Levy in 2023 and 2024 would provide dedicated funding for the tax levy contribution for YNSE

The Region's estimated capital contribution towards the YNSE is approximately $1.12 billion, however this amount has not yet been finalized by the Province, nor does it include any amount towards the Region's (as a "funding partner") oversight costs.

The 2022 Budget approved a 1% incremental Rapid Transit / Infrastructure Levy (RTIL) to help fund the tax levy component of the Region's share of the YNSE capital cost. As part of the 2022 Fiscal Sustainability Update in June 2022, Council directed staff, as part of the 2023 Budget process, to bring forward an option that continues the 1% annual tax levy increment to the RTIL for 2023 and 2024, to fund the tax levy contribution needed for the Yonge North Subway Extension. Total revenue from these proposed increases would cover the current estimated tax levy capital contribution for the YNSE as well as any "funding partner" costs.

A further incremental levy of 1% each year for 2025 and 2026 could be used to help fund new projects identified in infrastructure master plans

In 2022, the Region updated the Transportation Master Plan and the Housing York Inc. Board endorsed housing development projects for inclusion in the Region's Community Housing Development Master Plan. These exercises identified $2 billion in additional community housing needs and $5.4 billion to expand the Bus Rapid Transit network over the next 30 years. Additionally, changes to the Development Charges Act by way of Bill 23, the *More Homes Built Faster Act*, mean that Housing Services will no longer be eligible for development charge funding – this will result in a larger share of these projects requiring tax levy funding.

As the Region awaits commitment from senior levels of government, these projects continue through the preliminary engineering phases to ensure they are shovel ready when external funding is committed. The 1% incremental levy in 2025 and 2026 would allow the Region to ensure its portion of the funding needed would be ready when senior levels of government commit to these projects. Further increases could be required in future budget to address the impacts of Bill 23, *More Homes Built Faster Act.*

SOME MACROECONOMIC FACTORS HAVE CHANGED SINCE THE LAST FISCAL STRATEGY

Global economic recovery has led to higher inflation and a rapid rise in interest rates

As the global economy navigated the shocks caused by the COVID-19 pandemic, governments and central banks looked to support the economy through fiscal and monetary policy interventions. Macroeconomic pressures including supply chain issues and labour shortages have led to record levels of inflation, with the Consumer Price Index for Toronto reaching a high of 7.5% in July 2022 and Non-Residential Building Construction Price Index reaching 15.6% in the third quarter of 2022.

Over the course of 2021 to 2022, to help combat elevated inflation rates which were overheating the economy, the Bank of Canada raised the policy interest rate seven times from 0.25% to 4.25%, an increase of 1,700%.

Elevated interest rates will have an impact on the fiscal strategy through the capital and debt program.

In October 2022, the Province introduced Bill 23 which limits the Region's ability to fund growth-related infrastructure through development charges

Bill 23, the *More Homes Built Faster Act 2022,* was introduced in October 2022, and received Royal Assent on November 28, 2022. This omnibus legislation, aimed at increasing the supply of housing, amended nine Acts with varying levels of impact on the Region and introduces a new Act addressing wastewater servicing in York Region. The amendments to the *Development Charges Act, 1997* under this legislation will limit the Region's ability to

collect development charges (DCs) to fund future growth infrastructure as a result of new DC rate phase-in provisions, discounts, and exemptions as well as the removal of previously eligible costs such as housing services, growth studies and land acquisition. To maintain planned levels of capital expenditure, other sources of funding will be required.

4. Analysis

FIRST ELEMENT OF THE FISCAL STRATEGY – MANAGING THE CAPITAL PLAN

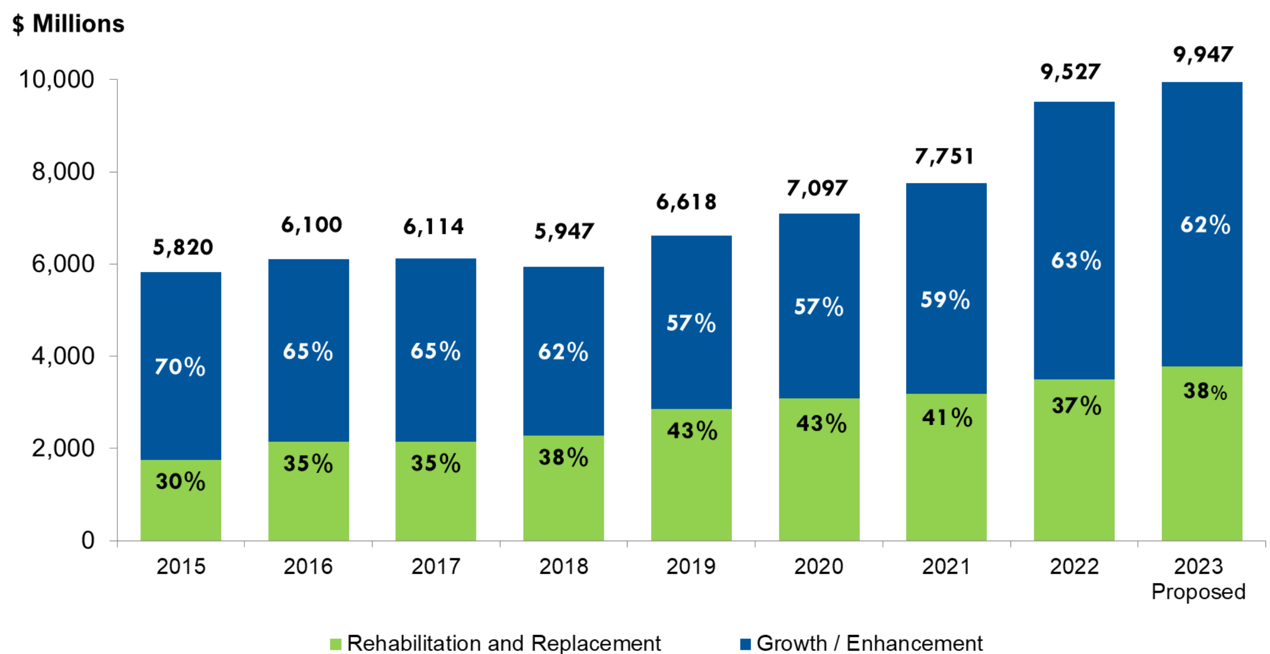
The Region continues to make significant investments in growth-related capital

The 2023 10-year Capital Plan is $9.9 billion. This includes approximately $6.2 billion in growth-related investment (including a projected $1.12 billion for the Region's contribution towards the YNSE) as well as a further $3.8 billion of asset rehabilitation and replacement spending. The proposed 10-year Capital Plan is $420 million higher than last year, as shown in Figure 2.

Development charges are the main source of funding for growth-related projects. However, the portion of projects that benefits existing residents cannot be paid for by development charges. Approximately $4.5 billion of the $6.2 billion spending is expected to be funded from development charges while the remaining $1.7 billion is expected to be funded from the tax levy and other sources as shown in Figure 3.

Figure 2

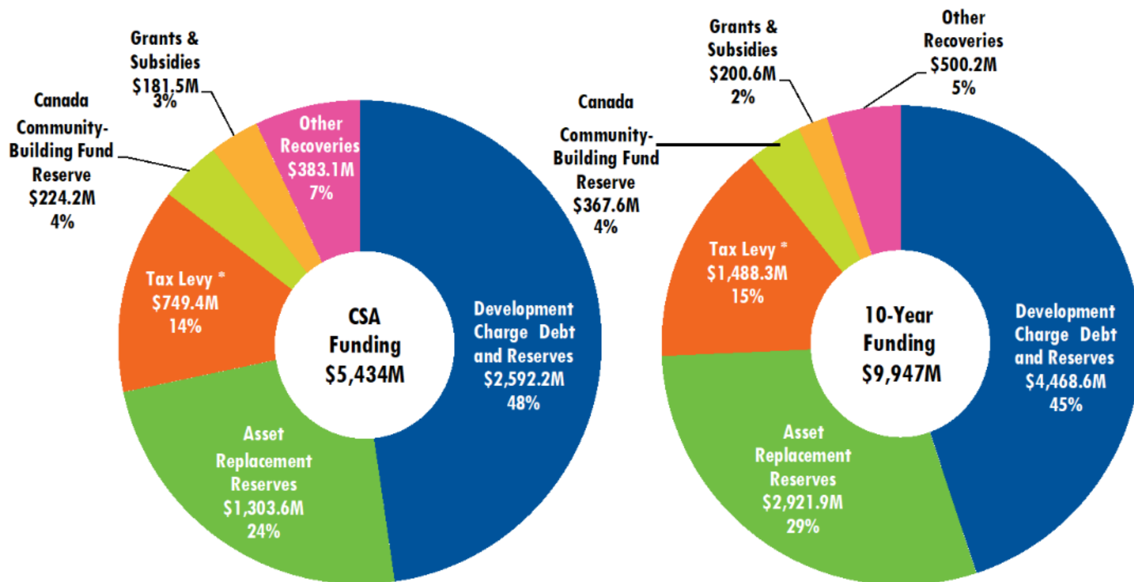
Comparison of 10-Year Capital Plans



Source: York Region Finance Department

Figure 3

2023 10-Year Capital Plan Expenditures and Funding Sources



*Tax Levy includes: Debt Reduction Reserve, General Capital Reserve, Program Specific Reserves, and Tax Levy Debt related only to the Zero Emission Transit Fund Program

Source: York Region Finance Department

Asset management spending is informed by departmental approved asset management plans

All departments have completed asset management plans that informed their long-term capital plans. Over the next 10 years, asset management spending is forecasted to be $250 million higher than last year's budget, mostly due to updated asset condition information provided as part of ongoing asset management assessments.

As was shown in Figure 3 above, $2.9 billion will be funded from asset replacement reserves, while the remainder will be funded from the Canada Community Building Fund (previously known as the Federal Gas Tax), recoveries, grants and other reserves.

$2.0 billion of projects related to community housing and bus rapid transit will be considered "below the line" under the 2023 10-year Capital Plan

In response to the fiscal constraints this year, staff undertook a capital prioritization exercise as part of the 2023 Budget process. As a result, projects that required a senior government contribution for which a commitment has not been received are deemed "unfunded" and have been presented as "below the line" in the 2023 10-year Capital Plan. These projects are related to bus rapid transit infrastructure and community housing totalling $2.0 billion over the next ten years.

These projects are not currently shown nor has any debt authority or capital spending authority been allocated to them. Should funding become available from senior levels of

government, the impact of adding these projects on the Region's long-term financial sustainability will be assessed.

SECOND ELEMENT OF THE FISCAL STRATEGY – RESERVE MANAGEMENT

By the end of 2022, the Region's reserves are expected to be approximately $4.3 billion, and contributions are largely on target

There are over 60 reserves and reserve funds that hold a combined total of approximately $4.3 billion as of December 31, 2022. Most of these will be used to fund future capital needs and have been grouped into the five categories shown in Figure 4.

The largest category, approximately $2.1 billion, will be for asset replacement. Growth capital reserves ($916 million) are the second largest component and include the Debt Reduction Reserve and funding for the non-DC portion of growth. The third largest component are corporate reserves, which include stabilization reserves. Development charges, considered to be deferred revenue rather than a reserve, are held separately, as required by law, to be managed along with development charge debt to fund growth-related capital projects.

The figures and discussion above do not include the Region's sinking fund reserve, which is a segregated fund that can only be used to repay existing debt. The amount in this reserve has been netted against the total outstanding debt to arrive at the "net" outstanding debt figure shown elsewhere in this report. The reserve consists solely of the cumulative amount of principal repayments that the Region made each year for existing debt as well as any interest earned on the balance. As of December 31, 2022, the balance in the sinking fund is approximately $1.1 billion.

Figure 4

Reserves and Reserve Funds as at December 31, 2022 and 2023 Planned Contributions

Reserve Balance ($Millions)	2022 Forecasted Balance	2023 Planned Contribution	2023 Contribution Target
Asset Replacement Tax Levy	1,383	161	Under Target
Asset Replacement User Rate	753	197	On Target
Subtotal: Asset Replacement	*2,137*	*358*	*Under Target*
Growth Capital	916	226	On Target
Development Charges	541	385	On Target
Corporate Reserves	671	47	On Target
Total	**4,263**	**1,016**	

Source: York Region Finance Department

Reserves are expected to continue to grow as the Region looks to build capacity to meet future asset management needs and fund the non-development charge portion of growth.

However, with the introduction of Bill 23, a portion of the contributions required for asset management may need to be diverted to help offset lost development charge revenues if there is no additional funding from senior governments and/or if there are insufficient tax levy and user rate increases to fund these shortfalls. Diverting required asset management contributions will further move the Region away from its progress towards intergenerational equity and may also limit the Region's ability to ensure its existing assets operate in a state of good repair.

Asset replacement represents the largest category of reserves but still needs to grow to meet future rehabilitation and replacement requirements

Asset replacement reserves are the largest category of the Region's reserves. Approximately $1.4 billion of these reserves are for tax levy-supported assets while the remaining $753 million is set aside for user-rate supported assets. Contribution targets have been set to ensure that new tax or rate supported debt will not need to be issued. The contribution targets use the estimated replacement value of the Region's assets, which now stands at over $19 billion, as identified in the 2021 State of Infrastructure Report. In addition, there is a further $4.9 billion of assets that is forecasted to be added over the next ten years. By 2032 almost $24 billion of assets will need to be rehabilitated or replaced and asset replacement reserves will need to continue to grow to fund this.

The projected contributions to tax levy-related asset replacement reserves are below the levels required to meet the needs of the Region's current and growing asset base over the long-term and currently place a greater strain on future generations to fund these needs. Additionally, several pressures may challenge the ability to grow these reserve balances in future years, including rising spending needs for asset management, growth capital including major infrastructure projects (e.g., YNSE, BRTs, community housing), operating budget pressures and the impact of Bill 23.

In 2021, Council approved updated User Rates that will achieve full-cost recovery in the water and wastewater sector and provide for full asset management contributions into the future.

While growth capital reserve contributions are currently on target for the projects in the 10-year Capital Plan, additional funding will be required for some new infrastructure projects and costs that are no longer eligible as a result of Bill 23

At the end of 2022, growth capital reserves, which are used to fund the portion of growth not covered by development charges, have a combined balance of $916 million.

As additional infrastructure projects are contemplated, including "unfunded projects" (e.g., bus rapid transit and community housing) and projects that are no longer eligible for development charges from Bill 23, growth capital reserves may face significant pressures to fund future needs. To meet these challenges, the 2023 Budget proposes an 1% additional incremental infrastructure-related tax levy increases for each of 2025 and 2026.

Growth capital reserves will not be able to meet any additional demands as a result of Bill 23 statutory discounts and exemptions without additional funding.

As implications of Bill 23 are not fully known at this time, it is recommended that staff report back on this matter as part of the 2023 Fiscal Sustainability Update

The proposed 2023 10-year Capital Plan was prepared mainly before the passage of Bill 23 and does not reflect any funding changes associated with it. Staff are continuing to analyze the impact of the changes, however a full assessment will not be possible until the Province issues regulations on several matters included within the Act. Initial estimates show that DC collections could be up to $1.6 billion lower over the next 10 years. Future budgets and fiscal strategies will need to address these reductions through one or both of adjustments to the size and timing of the capital plan and incremental tax levy and user rate increases above those recommended within this proposed multi-year budget. In addition to adapting to reductions in development charge collections, future budgets and fiscal strategies could be required to fund any additional or accelerated infrastructure spending required to support the objective of building 1.5 million homes in Ontario over the next 10 years.

Staff are awaiting clarity through the associated regulatory framework to refine the estimate of the overall financial impact. More information is anticipated to be shared in June 2023 as part of the Fiscal Sustainability Update Report.

Corporate reserves are in place to promote financial stability and flexibility

In addition to the capital reserves discussed above, the Region also contributes to corporate reserves, such as stabilization reserves and human resources reserves that contribute to financial stability and flexibility.

The stabilization reserves include the Tax Stabilization, Fiscal Stabilization, User Rate Stabilization, Fuel Cost Stabilization and Waste Management Stabilization reserves. They provide funding for unexpected expenditure or revenue shortfalls. The Pandemic Management Reserve is also included in this category. This reserve was created in 2020 to help fund COVID-19 related emergency costs.

Other corporate reserves include operating and human resource reserves to provide funding for their respective operating programs, and their targets are reviewed annually.

THIRD ELEMENT OF THE FISCAL STRATEGY – DEBT MANAGEMENT

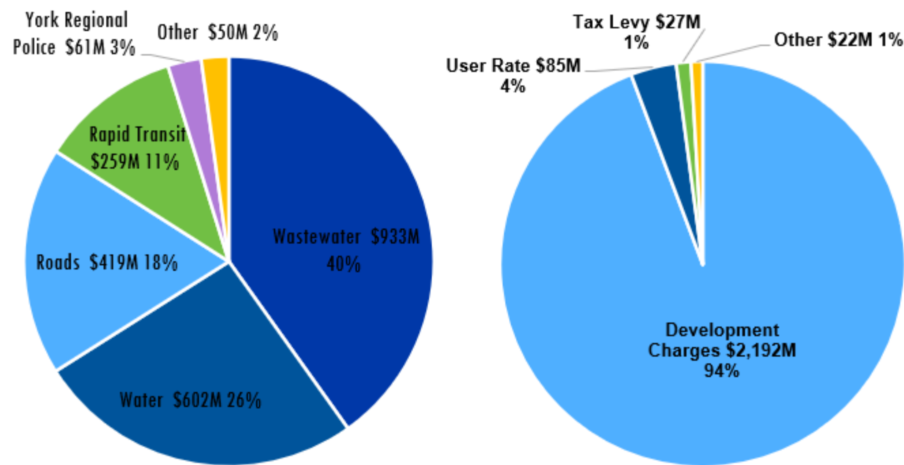
94% of the Region’s outstanding net debt is for growth-related infrastructure

Approximately 94% of debt outstanding at the end of 2022 is growth-related and will be funded through future development charge collections, as shown in Figure 5 below.

Figure 5

Outstanding Net Debt as at December 31, 2022

$2.3 Billion



Source: York Region Finance Department

74% of the projected Development Charge collections over the next 10 years will be required to service debt

Development charges are the main source of funding for growth-related infrastructure and are the sole source of funding for the repayment of principal and interest on existing and new debt issued for that purpose.

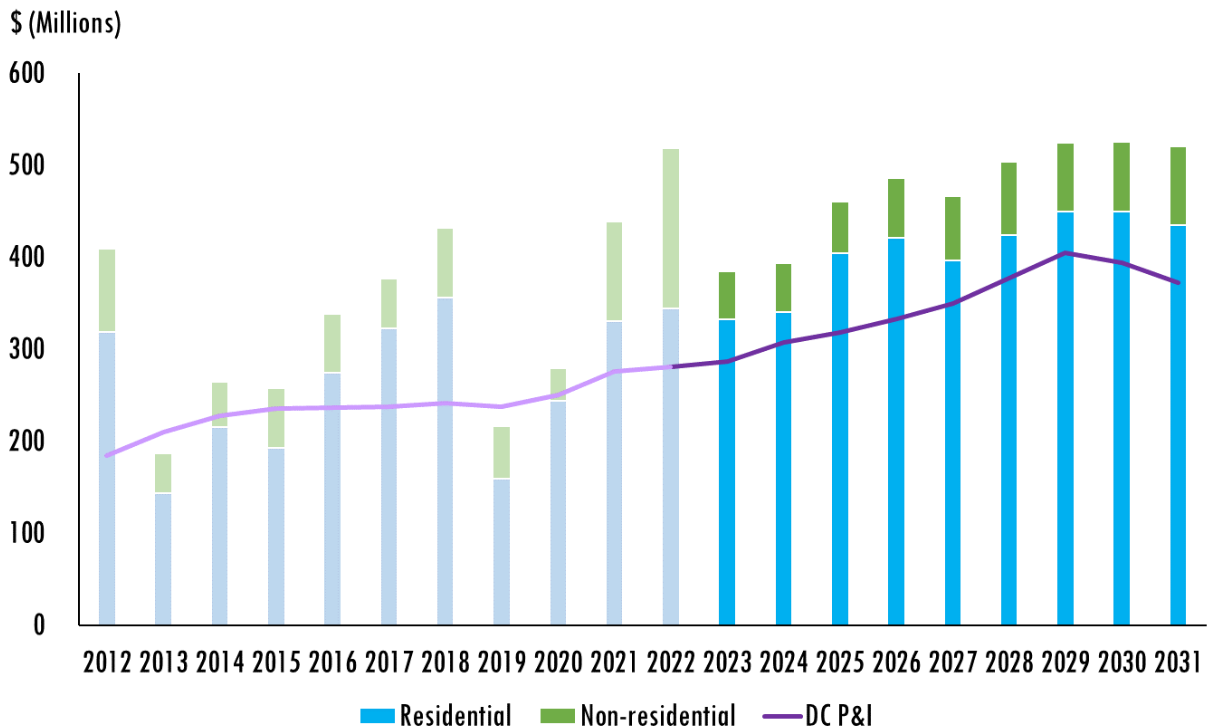
Figure 6 shows the comparison of forecasted development charge collections against the anticipated principal and interest payments for the proposed 10-year capital plan.

In 2022, the Region has collected $519 million in development charge collections (cash basis), just shy of the forecast of $530 million for the year. Over the next ten years, average annual development charge collections, which do not yet account for the impacts of the changes to the Act through Bill 23, are expected to be approximately $475 million. This forecast is predicated on continued robust levels of housing construction similar to the levels achieved over the past 10 years. During the same period, the average annual principal and interest payments are expected to be approximately $350 million per year.

This means that approximately 74% of forecasted collections will be needed to service the Region's debt, while the remainder is used to fund capital expenditures on a pay-as-you-go basis. It is anticipated that there will continue to be significant year-over-year fluctuation with collections, due to fluctuations in construction activities, changes in the economic cycle and changes in DC rates.

Figure 6

Historical and Forecasted Development Charge Collections and P&I



Source: York Region Finance Department
Note: DC Collections forecast does not reflect the impact of Bill 23 impact

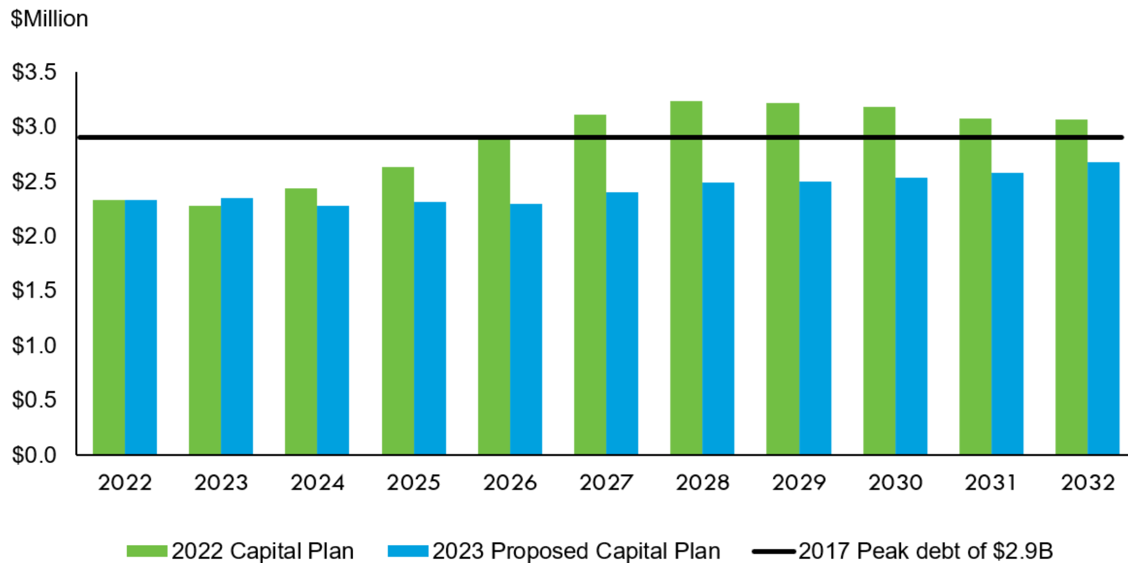
Projected debt levels are related to future growth infrastructure needs

Over the next ten years the Region will be required to pay approximately $2.7 billion in principal and interest for its existing debt. In addition, the 10-year Capital Plan projects further spending of approximately $6.2 billion on growth related infrastructure, for which the Region would need to issue approximately $3.0 billion in new debt over the same period.

The Region's net debt is expected to peak at $2.7 billion in 2032 which is lower than 2017's peak level of $2.9 billion. One of the key parameters considered by credit rating agencies is the level of debt and associated principal and interest costs. S&P requires debt servicing costs to be lower than 5% of the Region's operating revenue for a AAA credit rating. Managing the level of debt is key to ensuring the Region's borrowing costs remain below this threshold and a AAA credit rating is maintained.

Funding requirements for the 10-year Capital Plan, DC Collections and costs produce the debt profile shown in Figure 7.

Figure 7
Outstanding Net Debt Projection 2022 to 2032



Source: York Region Finance Department
Note: Outstanding Net Debt Projection does not include the impact of Bill

The level of debt for the 2023 10-year Capital Plan is projected to be lower than the 2022 10-year Capital Plan. This is necessary since the level of spending planned within the 2022 Capital Plan, especially considering rising interest rates, would have increased the Region's debt servicing costs above the 5% threshold needed for a AAA credit rating.

A significant part of the Region's Capital Plan is the YNSE. The cash-flow for the YNSE was updated by Metrolinx in 2022 and presents more certainty which allowed the Region to make required adjustments to the Capital Plan and reduce expected debt levels. This debt profile also helps to ensure that the Region's development charge collections are likely to exceed DC-funded costs each year of the 10-year Capital Plan making growth spending affordable.

A further analysis of the risks associated with debt, as well as the mitigation strategies used by the Region, are discussed in Section 3 of the 2022 Long-Term Debt Management Plan, included as Attachment 1.

A higher interest rate environment will make borrowing more expensive

Higher interest rates directly impact the cost of borrowing for the Region. As the Bank of Canada's policy rate increases, investors require a higher rate of interest on the Region's debt issuances. As discussed above, a key metric used by the credit rating agencies is the interest expense as a percentage of operating revenue. As interest rates increase, greater pressure is placed on this metric, and it could lead to a potential downgrade if debt levels aren't maintained at financially sustainable levels.

The higher interest rate environment has impacted borrowing costs for the Region. The average cost of 10-year borrowing has increased from 2.15% in the spring of 2021 to an estimated rate of 4.10% for 2023.The 2023 10-year Capital Plan, as submitted, has been optimized to ensure debt servicing costs remain sustainable, at the currently forecasted interest rates. However, should interest rates continue to increase, or do not abate as expected, further adjustments to the plan may be required.

CREDIT RATINGS

S&P and Moody's re-affirmed York Region's triple A credit rating

In 2022 both S&P and Moody's re-affirmed their credit ratings for the Region of AAA (stable) and Aaa, respectively. The credit rating agencies highlight the following strengths of the Region:

- Excellent liquidity profile with growing levels of cash and reserves
- Prudent and far-sighted fiscal management
- Continued strong fiscal outcomes
- Diversified and expanding economy

However, both rating agencies have expressed concern about the Region's elevated debt burden and associated debt servicing costs, especially relative to other rated Canadian municipalities. 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
- weak operating results

PROPOSED AMENDMENTS TO POLICIES

The Letter of Credit Policy needs to be amended to accept electronic Letters of Credit and update roles and responsibilities

Issued by financial institutions, a Letter of Credit may be requested by the Region to guarantee payment or provide financial protection from counterparties who fail to meet contractual obligations. The Region relies on Letters of Credit to provide purchase protection for certain types of purchases and contractual agreements. They are particularly important for high-value purchases that present elevated financial risk.

Letters of Credit are also requested from developers to guarantee development charge prepayments. Depending on the type of development, the Letter of Credit may be held, drawn in equal annual amounts or drawn completely following the achievement of a development milestone.

Letters of Credit received by the Region are forwarded to the Finance Department for safekeeping and administration. Electronic Letters of Credit have become more commonplace, and their use accelerated throughout the pandemic. Currently, the Region's Letter of Credit Policy is not clear in its treatment of electronic Letters of Credit. Staff recommend updating the Letter of Credit Policy to explicitly accept electronic Letters of Credit (see Attachment 3(a)). Staff also recommend updating some roles and responsibilities listed in the Letter of Credit Policy to better align with the current Finance organizational structure.

The Development Charge Interest Policy needs to be amended to reflect recent changes to the Act

Bill 108, *More Homes More Choice Act, 2019* introduced the ability for municipalities to charge interest on development charges installment payments and frozen development charges (under sections 26.1 and 26.2 of the Act respectively). At the time, the Province did not prescribe rules governing the charging of interest, nor a maximum interest rate. In response to this change Regional Council, in February 2020, approved the Region's Development Charge Interest Policy (Policy), which set out an interest rate of 5% per year. This rate was based on the average historical growth in the Statistics Canada Non-residential Building Construction Price Index for Toronto plus consideration based on the average historical fluctuation to the index to mitigate the risk of cost fluctuations to the Region.

However, as a result of Bill 23, the maximum interest rate that a municipality can now charge will be the average prime rate, charged by the five major banks in Canada, plus 1%.

As the Region's current Policy is to charge 5% and that there is strong justification to update that rate, using the methodology originally employed when developing the 2020 Policy, it is recommended that the Policy be amended to reflect the maximum allowable rate (see Attachment 3(b)). Aligning with changes to the Act is also a best practice the Region undertakes with its many other development charges policies as well as its development charges bylaws[1].

2023 LONG-TERM DEBT MANAGEMENT PLAN

Council affirmation of the 2023 Long-Term Debt Management Plan is required to access the growth-related borrowing capacity

Starting in 2011, the Province has provided a York-specific growth cost supplement that allows it to borrow a higher amount than what is permitted under the regular Annual Repayment Limit, based on its development charges collections. In 2013 and 2014, the

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[1] Note: For any developments that were issued a "Development Charges Rate Certificate" on, or after June 1, 2022, and prior to the date the revised policy comes into effect, and so long as a subsequent application is not made, an interest rate, the lower of the maximum permitted rate under section 26.3 of the Act and 5% shall be used until the development charges are fully paid.

Region could have breached the ARL in the absence of the growth-related cost supplement. In April 2021, the Province renewed the Region's growth-related cost supplement component of the ARL until December 31, 2031.

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 UPDATES TO RESERVES

Due to changes made to the Development Charge Act through Bill 23, it is recommended that two new reserves should be established to fund development charge shortfalls

As a result of the changes to the Development Charge Act through Bill 23, the Region is expecting annual shortfalls in development charge collections due to new statutory exemptions. To ensure the Region can continue to grow as planned, development charge collections will need to be made whole through alternative revenue sources. In preparation to meet these future needs, the following reserves are recommended to be established: the Tax Levy Development Reserve Fund and the Rate Supported Development Reserve Fund.

The purpose of these reserves will be to utilize tax levy and user rate revenues to offset annual statutory development charge collection shortfalls. These reserves are included in the Reserve and Reserve Fund Policy, in Attachment 2. As part of the Financial Sustainability Update, staff will provide a more fulsome analysis on the expected annual shortfall and the optimal funding of these reserves.

Reserve fund balances are reviewed annually to ensure adequate funds are available for future needs identified in the Capital Plan

The funding requirements of the 10-year Capital Plan are assessed annually alongside the projected balances in each reserve and reserve fund. Periodically, transfers between these reserves are required when funding sources change, or new needs are identified.

Table 1 provides an overview of the proposed balance transfers between capital reserves.

Table 1

Proposed Reserve Fund Transfers

Reserve Fund	Contribution to/(from)
Roads Infrastructure Reserve Fund	($25,300,000)
Roads Capital Acceleration Reserve Fund	$5,300,000
Transit Reserve Fund	$20,000,000
Non-Profit Housing Reserve Fund	($15,000,000)
Social Housing Development Reserve Fund	$15,000,000
Total	**-**

To fund the discretionary development charge exemptions made during the Bylaw ending June 2022, $29.8 million needs to be transferred from tax levy and user rate reserves to development charge reserves

Under the 2017 Development Charges Bylaw, which was in place until June 16, 2022, the Region provided a number of discretionary development charge exemptions that reduced revenues. These exemptions included the Cortellucci Vaughan hospital, places of worship, developments under 100 square meters and agricultural lands. Staff estimate that these exemptions totaled $29.8 million. Section 5(6)3 of the Development Charges Act, 1997, requires this shortfall must be funded through the tax levy and user rates. Table 2 outlines the draws and contributions required.

Table 2

Reserve Transfers to fund DC Discretionary Exemptions for DC Bylaw ending June 2022

Reserve Fund	Contribution to/(from)
Water DC	$189,518
Wastewater DC	$386,749
Roads DC	$21,110,231
Transit DC	$2,075,774
Subway DC	$3,564,065
Police DC	$1,919,113
Waste Diversion DC	$117,496
Paramedic Services DC	$274,160
Public Health DC	$39,166
Court Services DC	$78,331

Reserve Fund	Contribution to/(from)
Debt Reduction	($5,874,834)
Waste Management	($117,496)
Roads Capital	($21,110,231)
Transit	($2,075,774)
Water – Rate Stabilization	($189,518)
Wastewater – Rate Stabilization	($386,749)
Total	**-**

5. Financial

Under the fiscal strategy framework, the Region manages its capital plan, reserves and debt towards the goal of achieving long-term financial sustainability. The 2023 Fiscal Strategy sees 10-year capital investments amount to $9.9 billion, net outstanding debt peak at $2.7 billion in 2032.

6. Local Impact

Local municipalities will benefit from the fiscal strategy as it manages the Region's debt level and supports a superior credit rating. The debt issued by the Region represents a direct, joint and several obligations of the Region and local municipalities. As well, since local municipalities must issue all debentures 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 2023 Fiscal Strategy updates Council on the capital plan, reserves, and debt, and makes a number of recommendations, all intended to help the Region achieve financial sustainability.

The fiscal strategy is updated annually and evolves as circumstances change and as further analysis is incorporated.

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.

Recommended by: **Laura Mirabella, FCPA, FCA**
Commissioner of Finance and Regional Treasurer

Approved for Submission: **Bruce Macgregor**
Chief Administrative Officer

January 27, 2023
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14348553 - Attachment 1 – 2023 Long-term Debt Management Plan
14434186 - Attachment 2 – Reserve and Reserve Fund Policy
13954649 - Attachment 3 (a) – Letter of Credit Policy
14338977 - Attachment 3 (b) – DC Interest Policy