COUNTY OF WELLINGTON

COMMITTEE REPORT

To: Chair and Members of the Administration, Finance and Human Resources Committee
From: Ken DeHart, County Treasurer
Date: Tuesday, June 15, 2021
Subject: **Reserves and Debt Management Policies - Third Party Review**

Background:

In July of 2019, Council approved the County's Long-Term Financial Sustainability Policy and Strategy. The following represent the three pillars of resiliency identified in the Strategy:

1. **Financial Sustainability** – addresses the County stability. It is the ability to provide and maintain service and infrastructure levels without resorting to unplanned increases in rates or cuts to services.
2. **Financial Vulnerability** – addresses the County's vulnerability to external sources of funding that is cannot control. It is focused on minimizing the level of risk that could impact the County's ability to meet existing financial obligations and commitments, including delivery of service.
3. **Financial Flexibility** – is the County's ability to issue debt responsibly without impacting the County's credit rating or ability to generate required revenues. It is the County's capacity to change debt or tax levels to meeting financial obligations.

Strategic use of reserves and reserve funds and responsible debt management were identified as two of the nine financial principles and are an integral part of the Long-Term Financial Sustainability Strategy. In order to evaluate the performance of this strategy, key financial ratios and indicators were identified to be compared over time and across municipalities.

Over the last two budget cycles, County Council has inquired about the appropriate targets and balances in the County's reserves. The County participates in an annual municipal benchmarking study that compares municipalities representing over 85% of the province's population. County staff provide a summary report of these benchmarks annually during the budget process. In addition, Treasury staff contracted the BMA Municipal Financial and Management Consulting team to evaluate these key financial indicators that factor into a municipality's financial condition and review the County's policies and strategies that support financial sustainability – with an emphasis on the County's reserve and debt management policies. The consultant's report also provides information on municipal best practices and recommended actions.

The review includes a comparison to AAA-rated municipalities to provide a basis to better understand their financial position in relation to Wellington County and help identify any areas where policy modifications may be considered to further strengthen the County's credit rating and financial position. The County is also benchmarked with a broader comparator group that includes other Counties as well as the City of Guelph.

Summary of Findings:

Overall the County's financial condition is strong as demonstrated by our AA+ credit rating. Although it would be convenient to have one overall target for reserve balances as a percentage of taxes, the consultant's report stresses the need to examine reserve and reserve fund balance requirements by the three categories of contingency and stabilization, capital, and specific purpose reserves. Consistent with the Government Finance Officers Association (GFOA), the approach to reserves does not recommend a "one-size-fits-all" minimum target.

Strengths identified in the report include:

- A positive net financial position that is trending upwards indicating the County has the ability to cover debt obligations and have funds set aside for future sustainability.
- Total reserves and reserve funds as a % of taxation is trending up and exceeds the County's historical average of 80% of the tax levy.
- The County's Shared Services Stabilization reserve meets the minimum target to mitigate provincial or municipal cost sharing agreement changes.
- Capital reserves for solid waste and housing lifecycle replacements meet or exceed targets identified in the County's reserve policy.
- Overall capital reserve contributions and balances meet minimum targets in relation to general industry standards.
- Specific purpose reserve funds for Landfill Closure and Post-Closure, Workplace Safety Self Insurance and Post-Employment Liability are either fully-funded or very close to being fully-funded which demonstrates adherence to the Long-Term Financial Sustainability Strategy principle to protect and preserve intergenerational equity.
- Overall County debt management indicators are positive and below Provincial and County self-imposed levels indicating debt levels that are affordable to taxpayers.
- The County's debt-related financial indicators are below the average (but higher than the median) of Triple-A municipalities. The County is also relatively strong in comparison to the broader group. This indicates the County's debt levels compare favourably to most of its peers.

Potential Challenges include:

- The County's asset consumption ratio is higher than both municipal comparator groups, and has the worst ratio when compared Triple-A rated municipalities. This indicates that our assets are generally older than our comparators and we may be required to replace them sooner.
- Total reserve and reserve funds as a % of taxation, as a % of own source revenues and on a per capita basis indicate the County is below the average and median when compared to Triple-A rated municipalities and below the average on two out of the three indicators than the broader comparator group.
- The County's contingency and stabilization reserves are below the GFOA recommended target of no less than two months of own source revenues (16.7% of own source revenues) excluding the Winter Control and Shared Services Stabilization reserves.
    - The County's large geographic area prone to a harsh winter climate and significant reliance on external sources of funding (as a result of being the CMSM for Guelph-Wellington) would indicate a need for total contingency and stabilization reserves in excess of the GFOA minimum.
- Capital reserves for roads, property and ambulance do not meet minimum targets.

- When comparing capital reserve balances to the accumulated amortization of the County's assets as one best practice method of assessing adequacy of reserve levels, the County's capital reserves are well below the target of 100% (ideally the amount available in reserves at any time should equal the amount of our assets that have been depreciated or used up on a historical cost basis). However, this is consistent with most municipalities in Ontario when past generations did not fully contribute to reserves and infrastructure renewal, leading to an infrastructure deficit.
- The County's rates coverage ratio (own source revenue as a percentage of total expenditures) is the lowest when compared to the surveyed Triple-A municipalities and well below the mean and average of the broader comparator group. This indicates the County is more vulnerable to changes in upper levels of government funding or changes to shared services agreements and reinforces the need for higher levels of contingency and stabilization reserves.

Attachments:

- BMA Management Consulting Inc.- Financial Policy: Reserve and Debt Management 3rd Party Review

Next Steps:

County staff are currently undertaking extensive work on an updated Asset Management Plan (AMP) that will assist in the development of more refined capital reserve related targets for future budget processes. The AMP will incorporate condition assessments, full lifecycle costing and levels of service information.

Recommendation:

That the attached Financial Policy: Reserves and Debt Management 3rd Party Review from BMA Management Consulting be received for information.

Respectfully submitted,

Ken DeHart

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County Treasurer