

January 16, 2019

To: Members
Executive Committee

Re: Analysis of Reserve Establishment for Residential Road Renewal Program

RECOMMENDATION

1. That a reserve not be established for the Residential Road Renewal Program.
2. That the Residential Road Renewal Program Annual Report be enhanced to provide more clarity and comprehensive financial reporting, as outlined under Option 2 of this report.
3. That this report be forwarded to the January 28, 2019 meeting of City Council for approval.
4. That item EX18-11 be removed from the List of Outstanding Items for Executive Committee.

CONCLUSION

As directed by City Council (Council), Administration has researched and analyzed the benefits and implications of creating a reserve for the Residential Road Renewal Program (RRRP). Administration's understanding of the intent of this direction was to ensure comprehensive financial reporting and more clarity with respect to the use of the one per cent mill rate allocated to the RRRP and the Program in general. To meet this objective, two options were considered, including creating a reserve for the RRRP and enhancing the current annual reporting provided to Council on the status of the RRRP. Administration is recommending enhancements to the current annual report on the status of the RRRP (Option 2). This option would allow the City to effectively achieve comprehensive financial reporting. It is more efficient compared to Option 1, as it eliminates the extra administrative and Council effort associated with managing reserves, as well as transferring funds to and from reserves.

A reserve is not recommended for the RRRP because reserves are used primarily as a tool to set aside funds for future needs and to accumulate funds that are not yet allocated to projects. As all of the funding dedicated to the RRRP annually is fully allocated to projects, there would be no unallocated funding available to be transferred to a reserve, indicating that a reserve is not needed. If a reserve is created for the RRRP to transfer money that is allocated to projects but not yet paid out, Administration would have to take a report to Council whenever funds are needed from the reserve to pay for services. This process is time consuming and could potentially result in a delay in executing projects due to the administrative process of obtaining Council approval to use funds from reserves. Therefore, a reserve is not the most effective strategy to achieve more clarity and comprehensive financial reporting or to manage this program, as the implications of creating a reserve for the RRRP outweigh the benefits. The recommended Option allows unpaid but allocated funds (capital carry-forward) to remain in the project account. This capital carry-

forward, which is currently being calculated, will be reported and explained in the RRRP annual report (Option 2) as part of the enhancements to the report.

The recommended option allows Administration to effectively and efficiently meet the objective of comprehensive financial reporting with minimal administrative and Council effort, and it is also consistent with the treatment of funds allocated to capital projects at the City.

BACKGROUND

In 2014, Council recognized the need for a program which could affordably address the state of deterioration of the residential road network and bring it to an acceptable level. Based on Council direction, Administration developed the RRRP that reviewed the existing condition of the residential road network, created a road condition rating system and set potential levels of service (LOS) for this program, as well as reviewed financial scenarios with funding distributions for the different conditions of roads in the residential road network and their ability to achieve the established LOS.

As a result of this work, Council made a decision in 2014 to increase the budget of the RRRP through the allocation of a one per cent dedicated mill rate increase. In 2015, Council approved a longer-term strategy for the RRRP that would continue to dedicate a one per cent mill rate each year for five years (2015-2019). This funding was in addition to the allocation of 25 per cent of the existing Street Infrastructure Renewal Program's (SIRP) annual budget to the RRRP. This long-term strategy focused investments on preventative maintenance of the residential roadway network to help ensure affordability for residents over the entire life cycle of the asset. At that time, it was contemplated that a reserve may be established to manage this funding and provide ongoing reporting to Council. This option was not pursued because it was determined that a reserve would not be useful since all annual funding is allocated to projects. Reserves are typically used for funds that are not allocated to projects.

As part of the Reserve Review recommendations (CR18-54) approved by Council on May 28, 2018, Administration was directed to bring back a report to the Executive Committee outlining the benefits and implications of creating a reserve for the Residential Road Renewal Program.

The purpose of this report is to address the direction from Council.

DISCUSSION

To address Council's direction, this report is structured as follows:

- RRRP since implementation
- Objective of considering a reserve for the RRRP
- Criteria for assessing a reserve for the RRRP
- Options, benefits and implications of achieving more clarity and comprehensive financial reporting for the RRRP

Residential Road Renewal Program since Implementation

The RRRP was developed in 2014 with the goal of achieving a level of service of 85 per cent of the residential road network in “fair” or “better” condition over 25 years through a preventative maintenance strategy. The RRRP is funded through the allocation of a one per cent mill rate dedicated to this program in addition to the 25 per cent of the SIRP. The 2014 mill rate allocation of one per cent was preserved as the base funding for the residential road improvement and the subsequent mill rate allocation of one per cent for five years, including 2019, has been added incrementally to that base funding. It is expected that after 2019, the one per cent incremental mill rate allocation will stop but the base funding including the 2019 allocation, will continue to be dedicated to this program.

From 2014 to 2018, \$45 million has been invested in residential roads. The City has undertaken 300 projects to treat residential roads covering 87 kilometers or 13 per cent of the residential roads network. The City allocates the total program budget for the year to projects based on priorities and Council approved policies. Some projects may not be fully completed during the year due to weather, scheduling constraints, or increased scope of work. The allocation to such projects would not be paid out in the current year until the project is complete, resulting in the balance of the allocation being carried forward into future years. It is important to note that the carry-forward amount is already committed to multi-year projects to be spent in future years and cannot be reallocated without impacting in-progress projects.

Administration's 2019 recommended budget includes the final year of the one per cent mill rate allocation totalling \$12.0 million and a total program budget of \$16.3 million, including the 25 per cent allocation from the SIRP. In 2020 and beyond, the base budget will remain at this level, as the one per cent incremental mill rate will no longer apply based on the current Council consideration.

Objective of Considering a Reserve for the Residential Road Renewal Program

The intent of Council in directing that the benefits and implications of creating a reserve for the RRRP be analyzed was to ensure comprehensive financial reporting and more clarity with respect to the use of the one per cent mill rate allocated to the RRRP and the Program in general. It is also Administration's understanding that Council specifically had an interest in understanding the amount of the unspent funds (capital carry-forward) in this Program at year-end with rationale as to why the funds are unspent. While Administration provides an annual report to Council on the status of the RRRP, there is an opportunity to enhance this reporting to achieve greater financial reporting.

Criteria for Assessing a Reserve for the Residential Road Renewal Program

The City's Reserve Policy specifies that all new reserves be assessed against the criteria for creating reserves to determine whether a reserve should be established. The criteria for creating reserves are highlighted below and they seek to address the following questions:

- (a) **Alignment to City Priorities** - How well does a reserve support the achievement of the City's priority and business needs?
- (b) **Purpose of Reserve** - How does the reserve support the achievement of general purposes of the City's reserves (asset management, financial stability, financial flexibility and new capital acquisition)?
- (c) **Funding Strategy** - Is a reserve the most appropriate funding strategy for the City's business need?
- (d) **Funding Source** - Will the reserve be funded primarily from external user fees/charges/rates or through property tax revenues?
- (e) **Impact on General Fund or Mill Rate** - What financial impact will the reserve have on the general fund revenue or the mill rate?
- (f) **OCP Principles** - How well does the reserve support principles in the OCP such as the benefits model or cost recovery?
- (g) **Transparency** - Will the creation of a reserve help to provide greater transparency in the allocation, use and reporting of funds?

The RRRP was assessed against these criteria. Overall, the assessment shows that a reserve meets some of the criteria such as enhancing transparency and supporting the City's asset management and financial stability. However, the assessment also shows that establishing a reserve for the RRRP is not the most appropriate strategy to achieve the intended Council objectives and the business needs of this Program. Two key reasons why a reserve does not support the business needs are:

- Reserves are created to set aside funds that are typically not yet allocated to projects. As the RRRP funding is fully allocated to in-progress projects, there would be no unallocated funding available to be transferred to the reserve. This means this Program does not meet the definition of a reserve.
- Creating a reserve for the RRRP is not the most efficient way to meet Council needs as it could lead to additional work for both Council and Administration as highlighted below:
 - Reconciling transactions related to the RRRP, at year end
 - Transferring unspent but allocated funds from the RRRP to the reserve, at year end
 - Preparing reports to Council to transfer funds from the reserve whenever funds are needed to pay for completed projects

This process could be time consuming and is inconsistent with the City's current process of managing funds allocated to capital projects. This could potentially result in a delay in executing projects due to the administrative process of obtaining Council approval to use funds from reserves. A more effective and efficient approach of achieving more clarity and comprehensive financial reporting for the RRRP is articulated in Option 2 below.

Options, Benefits and Implications for Achieving Comprehensive Reporting for the RRRP

Two options for achieving more comprehensive financial reporting and clarity for the RRRP are analyzed as follows:

1. Option 1: Create a reserve for the RRRP

2. Option 2: Enhance the RRRP annual reporting to Council

Option 1: Create a Reserve for the RRRP (Not Recommended)

This option requires creating a reserve to track any unspent funds for the RRRP. It would ensure that an annual report on the reserve balance be provided to Council in accordance with the annual reserve reporting requirements specified in *The Regina Administration Bylaw*, Bylaw No. 2003-69.

Benefits:

- Ensures separate tracking and reporting of funds dedicated to improving the residential road network.
- Enhances public accountability and comprehensive reporting in the use of resources.

Risks/Implications:

- Reserves are used primarily to set aside funds for future needs. The RRRP is an annual program that requires ongoing investments, and the expectation is not to accumulate money for future expenditure. Therefore, there is no strong rationale for creating a reserve for the RRRP.
- Reserves are also typically used to accumulate funds that are not allocated to projects. The RRRP annual funding is fully allocated to projects and unspent funding for projects that are not completed during the year are considered “capital carry-forward” and allocated to completing the project in the next year. Capital carry forward from the RRRP is not available to be transferred to the reserve as the funds are already committed to ongoing projects. Therefore, it would be redundant to create a reserve for the RRRP as there may not be unallocated funding to be transferred to the reserve.
- Creating a reserve for the RRRP would be inconsistent with the City’s current practice where similar ongoing programs funded through the mill rate, such as the Street Infrastructure Renewal Program, Bridge Infrastructure Program, etc. are not managed through a reserve.
- If a reserve is created for the RRRP to transfer money that is allocated to projects but not yet paid out due to the project not being completed, Administration would have to take a report to Council whenever the funds are needed from the reserve to pay for services. This creates additional work for Council and Administration, and it could potentially result in a delay in executing projects due to the administrative process of obtaining Council approval to use funds from reserves.
- It may result in duplication of effort as the information to be provided through the annual reserve report can be provided through the current reporting to Council discussed in Option 2.

Option 2: Enhance the Residential Road Renewal Program Annual Report (Recommended)

This option would provide an improvement to the current annual reporting to Council on the status of the RRRP. The current report will be enhanced to clarify existing information and provide additional information as noted below.

- a) Separately identify the RRRP budget¹ components, any capital carry-forward amount from the previous year, actual expenditures and any capital carry-forward amount at the end of the year, including an explanation of the nature of the capital carry-forward (i.e. whether the capital carry-forward is committed or not yet allocated to projects) and why it is not yet spent.
- b) The RRRP budget, actuals and capital carry-forward amount since implementation of the RRRP.
- c) A description of the number of kilometres of road and number of projects planned and completed during the year.
- d) A description of the number of kilometres of road and number of projects planned and completed since the implementation of the RRRP.
- e) A list and an explanation for any projects that were not completed during the year and a plan that will ensure those projects are completed, including schedule.
- f) A description of the overall funding for the RRRP compared to the long-term goal of achieving 85 per cent of the residential road network in “fair” or “better” condition, and any funding gap.

It is important to note that while the majority of this information is currently being provided, items ‘e’ and ‘f’ as well as information related to ‘capital carry-forward amount’ are not being provided and are part of the recommended enhancements to improve the RRRP annual report to Council. Reporting and explaining the capital carry-forward amount would achieve the same objective as a reserve. In addition, the overall structure of the RRRP annual report would also be improved to ensure better information and understanding.

Benefits:

- Improves the current annual reporting to Council on the status of the RRRP.
- Enhances public accountability and comprehensive reporting. The RRRP annual report will contain more relevant information such as those mentioned under items ‘e’ and ‘f’ above, including the capital carry forward amount, which is not currently being reported to Council.
- Ensures efficient use of resources associated with managing and reporting on reserves.

Risks/Implications:

- Requires minimal administrative effort to develop improved reporting on the RRRP compared to Option 1.

¹ This includes the annual mill rate allocation plus the 25 per cent allocation from the Street Infrastructure Renewal Program budget.

RECOMMENDATION IMPLICATIONS

Financial Implications

There are no expected financial implications or risks arising from the recommended policy option (Option 2). The recommended option will ensure more comprehensive financial reporting and enhance clarity in the use of the dedicated funding for the RRRP. This supports the targeted outcome of the City's strategic plan of ensuring "residents trust the City by being informed and engaged".

Environmental Implications

None related to this report.

Policy and/or Strategic Implications

Overall, the recommendation allows Administration to efficiently and effectively achieve Council's objective of greater public accountability and clarity in the management of the RRRP. The RRRP is consistent with the corporate asset management as outlined in *Design Regina: The Official Community Plan (OCP)*. It supports the City's strategic plan of improving the development and maintenance of livable neighbourhoods while enhancing the residential road infrastructure condition to a level and quality that is sustainable. Ensuring comprehensive financial reporting and more clarity in the use of the dedicated funding for the RRRP is also consistent with the City's priority of achieving long-term financial viability as identified in the OCP.

Legal Implications

None related to this report.

Other Implications

None related to this report.

Accessibility Implications

None related to this report.

COMMUNICATIONS

None related to this report.

DELEGATED AUTHORITY

The recommendations contained in this report require City Council approval.

Respectfully submitted,



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Respectfully submitted,



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