

FINANCIAL MANAGEMENT

Effective Date: October 26, 2018

Approved By: MVRD/GVWD/GVS&DD/MVHC Boards

Policy No. FN-026

PURPOSE

To establish the principles that will guide decision making with respect to funding long term operating and capital expenditures for the Greater Vancouver Water District (GVWD), Greater Vancouver Sewerage and Drainage District (GVS&DD), the Metro Vancouver Regional District (MVRD) and the Metro Vancouver Housing Corporation (MVHC).

DEFINITIONS

“Operating Expenditures” are the costs that are incurred consistently year to year in the delivery of services including labour costs and the day-to-day costs related to staff support, utilities, equipment usage, supplies and the ongoing maintenance of assets and infrastructure, as defined under Generally Accepted Accounting Principles. These are expenditures where the value is realized and charged against revenue in the year incurred;

“Capital Expenditures” are costs that are incurred for expanding, enhancing, upgrading and replacing infrastructure used in the delivery of services as well as the purchase of equipment. These are expenditures where the value is realized for multiple years. These expenditures are treated as assets where the realization of their utilized value is charged to revenues proportionately over their useful life; and

“Debt Amortization” is the term over which a debt obligation will be repaid.

POLICY

As the primary regional service and utility provider for the region, Metro Vancouver is responsible for ensuring that the services it delivers provide value to its member jurisdictions, to its businesses and to its residents. Ensuring this value is achieved for ratepayers over the long term requires an adherence to sound fiscal policies that balance equity, affordability and continuous improvement through responsible fiscal management.

This Policy supports Metro Vancouver’s mandate by establishing sound financial management parameters that will guide the implementation of Metro Vancouver’s long term financial plan for its four Metro Vancouver legal entities.

1. FINANCIAL MANAGEMENT PRINCIPLES

Metro Vancouver’s financial management approach is to balance between two sources of funding for operating and capital expenditures incurred by the legal entities and functions comprising Metro Vancouver:

- pay-as-you-go funding
- long-term debt funding

The approach of relying on these two sources of funding is consistent with the requirement of maintaining a sound financial position for Metro Vancouver's four legal entities while also ensuring that they are fiscally sustainable in the long term.

The objective is to strike a balance between the ability of ratepayers to 'pay-as-you-go' for operating and capital expenditures and the need to secure long term financing for expenditures with a significant financial burden or that form part of a long term capital infrastructure program. It is critical to ensure that the level of long term borrowing does not exceed accepted fiscal parameters which would result in a greater burden on ratepayers in the long term than the benefit derived by this debt.

To achieve the financial management objectives described above, the following principles are established for all Metro Vancouver functions:

- Funding of ongoing and recurring expenditures directly in the year in which they are incurred;
- Funding from Reserves in accordance with the *Operating, Statutory and Discretionary Reserves Policy*;
- Funding of expenditures matches the realization of the benefit from those expenditures when expenditures are not ongoing or recurring;
- Consistency with legislative requirements;
- Financial flexibility to meet future financial requirements; and
- Mitigation of current and future financial risk.

Fundamental to the application of these principles is to ensure the necessary balance between fiscal sustainability and the financial impact on current and future ratepayers of the region.

a) Pay-As-You-Go Funding

Using pay-as-you-go funding, annual operating and capital expenditures are funded directly through annual revenues from user rates, fees, levies and requisitions or through the application of reserves in accordance with the *Operating, Statutory and Discretionary Reserves Policy*. Prudent financially sustainable funding includes:

- Funding ongoing and recurring expenditures directly in the year in which they are incurred; and
- Matching the funding of expenditures with the realization of the benefit from those expenditures when expenditures are not ongoing or recurring.

BOARD POLICY

Operating expenditures are, by their nature, generally ongoing and recurring and when they are not, the benefit is realized in the year incurred; therefore, operating expenditures will always be funded on a pay-as-you-go basis.

Where specific reserves exist to fund capital expenditures, capital expenditures should be funded on a pay-as-you-go basis from those Reserves in accordance with the *Operating, Statutory and Discretionary Reserves Policy*. These capital expenditures include MVHC capital replacement, laboratory equipment, Park Land acquisition, Parks infrastructure, Air Quality monitoring equipment, Head Office improvements, computer hardware and fleet vehicles.

Capital expenditures that are not generally funded through Reserves will be funded on a pay-as-you-go basis at a minimum annual level that represents the amount of total capital expenditures incurred consistently from year to year.

b) Long-Term Debt Funding

Long-term debt funding will only be used to fund capital expenditures. More specifically, those capital expenditures not funded from Reserve and in excess of the amount of total capital expenditures incurred consistently from year to year which are funded on a pay-as-you-go-basis.

c) Pay-As-You-Go Vs Long-Term Debt Funding

Funding capital expenditures on a pay-as-you-go basis and avoiding long-term debt funding provides significant benefits to Metro Vancouver. The avoidance of debt eliminates the risk associated with fluctuating interest rates, reduces the overall cost to the organization through the savings of interest payments and provides financial capacity should unforeseen funding needs be required. In addition, the funding of this consistent level of capital expenditures annually provides a measure of generational equality whereby each generation pays their consistent share.

d) Debt Service Level

To achieve pay-as-you-go funding to a level of consistent annual capital expenditures, pay-as-you-go funding will be gradually increased over time such that the amount of annual revenues required to pay for debt service cost does not exceed 40%. This balances the inherent risk associated with borrowing with the financial flexibility needed to meet financial requirements and manage the regions assets in an affordable manner and consistent with the principles of this Policy.

e) Debt Amortization Period

Long-term debenture financing procured by Metro Vancouver will be amortized over 15 years. The shorter amortization term reduces the risk associated with interest rate fluctuations over the term of the debt, reduces the overall cost by reducing the total amount

of interest paid and by retiring the debt sooner, Metro Vancouver has more financial flexibility to absorb new financial requirements.

2. METRO VANCOUVER FINANCING

a) GVWD, GVS&DD and MVRD

Where debt funding is deemed appropriate in accordance with this Policy, financing for GVWD, GVS&DD and MVRD projects will be obtained through long-term debenture financing procured through the Municipal Finance Authority (MFA) which is available twice per year, March and October.

Long-term financing. Long-term debenture financing requires the repayment of the debt obligations through a combination of principal repayments and interest payments. Principal repayments, paid annually, are based on a sinking fund methodology where payments are deposited into an interest earning sinking fund and at the end of the debt term the combination of principal repayments and interest earned is sufficient to retire the outstanding debt obligation. The amount of the principal repayment amount, paid annually, is actuarially determined based in the debt term or amortization and the expected earnings of the sinking fund. Interest, paid semi-annually, is based on the financing terms as determined by the financial markets.

Short-term financing. The capital expenditures incurred between times when long-term financing is available will be funded on a short-term basis either through the MFA or through the usage of internal savings. Short-term financing requires payments to cover interest only. Long-term debt funding will not be procured in advance of incurring capital expenditures unless specifically authorized by the Board.

DCC funding. In the GVS&DD Liquid Waste function, annual debt service costs for long-term debt associated with capital expenditures for infrastructure growth projects are funded using Development Costs Charges in accordance to the *GVS&DD Development Cost Charges Bylaw*.

b) Metro Vancouver Housing Corporation (MVHC)

Capital expenditures for the MVHC are those associated with the development of new affordable housing units. The MVHC maintains a development reserve in order to provide partial funding of development and redevelopment opportunities.

The MVHC development expenditures are funded through a combination of funding from the MVHC Development Reserve applied in accordance with the *Operating, Statutory and Discretionary Reserves Policy*, any funding received from other levels of government and traditional mortgage financing. The level of mortgage financing, either through the Province or Financial Institution, is determined based on the maximum annual mortgage payment amount and amortization period that can be supported by the applicable tenant rental revenue.

BOARD POLICY

Each development and redevelopment opportunity will be evaluated on its own merits financially in terms of the rental revenue expectations along with the appropriate combination of funding.