

FINANCE COMMITTEE REPORT

Report Date	November 26, 2018
Meeting Date	December 06, 2018

Chairman David Merrithew and members of the Finance Committee

SUBJECT: RESERVE FUND

OPEN OR CLOSED SESSION

This matter is to be discussed in open session of Finance Committee.

AUTHORIZATION

Primary Author	Commissioner/Dept. Head	City Manager
<i>Hilary Nguyen</i>	<i>Kevin Fudge</i>	<i>Neil Jacobsen</i>

RECOMMENDATION

Staff recommend that Finance Committee recommend to Common Council to approve the transfer of:

- \$400,000 to an Operating Reserve to cover the potential increase in WorkSafeNB premiums;
- \$400,000 to the General Capital Reserve to fund infrastructure deficit;
- \$500,000 to an Operating Reserve to fund the demolition of the Coast Guard Administration Building in 2019;
- \$100,000, which is the amount needed to complete the Market Slip Dredging to an Operating Reserve to be used in 2019;
- \$1 Mil which is the projected surplus in the Utility Operating Fund to the SCDW project reserve fund;
- Any fluctuation in the value of the City's employee benefit programs due to actuarial gains to an Operating Reserve annually in order to fund future losses;
- Approve the "Reserve Schedule A" included in this report.

EXECUTIVE SUMMARY

The Reserve Policy was approved by Common Council on December 11, 2017. The purpose of the Reserve Policy is to address longer term funding strategies to minimize debt servicing costs, address the infrastructure deficit, and mitigate the effect of unanticipated events. Permitted uses of reserves according to the Reserve Policy are:

- 1 Major unanticipated/unforeseen events;
- 2 Major Capital renewal;
- 3 Future Liabilities;

- 4 One time operating expenses which are greater than \$100,000 and are not part of the recurring operating budget;
- 5 Infrastructure deficit; and
- 6 Investment in growth opportunities.

In addition to the Reserve Policy, the City has to comply with the Provincial Reserve Fund Regulation which prescribes that the establishment, funding and withdrawal of Reserve funds can only be done through resolutions of Common Council before the end of each calendar year.

In alignment with the City's Reserve Policy, this report includes recommendations to transfer:

- \$400K to an Operating Reserve for WorkSafeNB premiums increase;
- \$400K to the General Capital Reserve to fund Infrastructure deficit;
- \$500K to an Operating Reserve to fund the demolition of the Coast Guard Administration Building in 2019;
- \$100K to an Operating Reserve for the completion of the Market Slip Dredging in 2019;
- \$1 Mil to the SCDW project Capital Reserve;
- Any fluctuation in the value of the City's employee benefit programs due to actuarial gains to an Operating Reserve annually in order to fund future losses.

To comply with the Provincial Legislation, Staff recommend that Common Council approve the total amounts of contribution to and withdrawal from the Reserves as detailed in the Schedule A included in this report.

PREVIOUS RESOLUTION

[Click here to enter any previous relevant resolution.](#)

STRATEGIC ALIGNMENT

This report aligns with Council Priorities.

REPORT

The Reserve Policy was approved by Common Council on December 11, 2017. The purpose of the Reserve Policy is to address longer term funding strategies to minimize debt servicing costs, address the infrastructure deficit, and mitigate the effect of unanticipated events. Permitted uses of reserves according to the Reserve Policy are:

- 1 Major unanticipated/unforeseen events;

- 2 Major Capital renewal;
- 3 Future Liabilities;
- 4 One time operating expenses which are greater than \$100,000 and are not part of the recurring operating budget;
- 5 Infrastructure deficit; and
- 6 Investment in growth opportunities.

In addition to the Reserve Policy, the City has to comply with the Provincial Reserve Fund Regulation which prescribes that the establishment, funding and withdrawal of Reserve funds can only be done through resolutions of Common Council before the end of each calendar year.

Currently, the City has the following reserves:

- **Operating Reserves:**
 1. General Operating Reserve
 2. Growth Reserve
- **Capital Reserves:**
 1. General Capital Reserve
 2. Fleet Reserve – General Fund
 3. Fleet Reserve – W&S Utility Fund
 4. Computer Reserve
 5. Utility Capital Reserve for Safe, Clean, Drinking Water Project
 6. Utility Infrastructure Reserve.

The reserves have been managed in accordance with the Reserve Policy. During the year, withdrawals from the reserves were approved by Council in advance on a case by case basis and the reserves have been used for their intended purposes.

Reserve for Workers' Compensation:

In November, WorkSafeNB announced that the Workers' Compensation rate will go up and the increase is likely to be significant. The impact on the City's budget can be as high as \$1 Mil. It is difficult for the City to absorb the full cost in one year, therefore, Staff recommend that the City transfer \$400K from the City's contingency budget to an Operating Reserve to fund future increases in Workers Compensation premiums.

Reserve for Infrastructure deficit:

Based on the City's 2016 State of the Infrastructure Report (SOTI) prepared by R.V Anderson in August 2017, the infrastructure deficit for the General Fund was estimated at \$219.4 Mil. Although the estimate was done at a high level, it reflects the magnitude of infrastructure backlog due to insufficient capital funding over many years. Staff recommend that \$400K from the 2018 projected

surplus be transferred to the General Capital Reserve to fund Infrastructure deficit.

Reserve for Market Slip Dredging

The City budgeted \$142K for the Market Slip Dredging in 2018. The project is underway, however, will not be completed before the end of the year. Staff recommend that \$100K be transferred to an Operating Reserve to pay for the outstanding portion of the project in 2019.

Reserve for Fluctuations in Employee Benefit Programs due to Actuarial Gains or Losses:

Pursuant to the Public Sector Accounting Standards, the City is required to have actuarial valuations done for the City's benefit programs such as Heart & Lung, Retirement Pay or disability pensions at the end of each year to determine the value of the City's liabilities associated with the employee benefit programs. The actuarial valuations have been done by a Professional Firm called "Aon". As a result of the actuarial valuations, the value of the City's liabilities related to the employee benefit programs can fluctuate due to various factors among which is the discount rate. If the discount rate goes up, the value of the liabilities will go down and vice versa. The accounting entries to record these fluctuations can cause significant negative or positive impacts to the City's budget. For example, the impact of the benefit true-up entries was a \$1.5 Mil charge to the City's budget in 2014. For 2018, staff was advised that it is likely that the discount rate at December 31, 2018 would go up 0.40% compared to 2017 which may result in a positive impact on the City's budget of \$600K-\$800K. Given the actuarial gains or losses are unrealized and the fluctuation in discount rates is beyond control of the City, Staff recommend that going forward all actuarial gains be put in an Operating Reserve to offset future actuarial losses.

Saint John Water projected surplus:

Saint John Water has prepared a year end projection based on actual results at October 31, 2018 and estimated revenue and expenditures for the remaining two months. The Utility is currently estimating a surplus of \$1,138,257 (2.38%) variance for the year. Meter revenue continues to have the largest variance along with interest revenue which is due to higher interest rates than budgeted for. Drinking water has the largest variance and is mainly due to earlier than anticipated startup of the Eastside Water Treatment plant.

Due to the outstanding financial risk of the Safe Clean Drinking Water project; staff recommend that \$1 Mil of the operating surplus be transferred to the SCDW reserve fund.

The following schedule summarizes the amounts of contribution made to and withdrawal from each reserve account and the projected balance of each account at the end of the year. It is important to note that the numbers in the schedule below include estimates for November and December transactions and an assumption that Council approves the above reserve recommendations. Therefore, the final numbers can be different from the estimates.

Reserve Schedule A				
Reserves	Opening Balance (\$)	Contribution to (\$)	Withdrawal from (\$)	Ending Balance (\$)
General Operating Reserve	3,123,777	1,057,732		4,181,509
Benefit Fluctuation Reserve		600,000		600,000
Growth Reserve	183,000	350,000	49,980	483,020
General Capital Reserve	1,100,000	420,330		1,520,330
Fleet Reserve - General Fund	1,255,650	2,655,298	1,249,132	2,661,816
Fleet Reserve - Utility Fund	915,377	510,519	97,359	1,328,537
Computer Reserve	1,151,092	1,029,530	631,390	1,549,232
SCDW Utility Capital Reserve	12,357,232	6,569,887		18,927,119
Utility Infrastructure Reserve	313,905	5,801		319,707
Total	20,400,033	13,199,097	2,027,861	31,571,269

Due to the timing of vehicle deliveries and cash flow, fleet reserve balances at year end are higher than projected. However, the fleet reserve balances will go down once vehicles are delivered and payments are made. The SCDW Utility Capital Reserve will be used up next year once the project is substantially completed. The General Capital Reserve will be used for the City Hall renovation and fit-up as approved by Council in the 2019 Capital Budget. The General Operating Reserve will be used to pay for the Coast Guard site Administration building demolition and the Market Slip dredging. As a result, the City's total reserve balance is projected to be significantly lower at the end of 2019.

SERVICE AND FINANCIAL OUTCOMES

This report is aligned with Common Council's approved Reserve Policy.

INPUT FROM OTHER SERVICE AREAS AND STAKEHOLDERS

Input has been received from other service areas.

ATTACHMENTS

List attachments related to report.