2015-2024 Capital Investment Agenda

Recommendation:

1) That the draft 2015-2018 Capital Budget be developed based on fully funding the Risk-based Infrastructure Management System infrastructure renewal target.

2) That the Capital Project Prioritization Criteria for Growth Projects in Attachment 5 of Financial Services and Utilities report CR_1258, be used as a basis to score and rank growth projects for the draft 2015-2018 Capital Budget.

3) That the arterial roadway renewal funding for the 2015-2018 period be no less than $55 million per year.

Report Summary

This report provides an introduction to the 2015-2024 Capital Investment Agenda and provides Council an information foundation in advance of preparing the 2015-2018 Capital Priorities Plan.

Report

The 10-Year Capital Investment Agenda is developed by Administration and will be updated every four years to coincide with the 4-year Capital Priority Plan.

The Capital Investment Agenda looks at capital planning and future investment requirements from a corporate vantage point. The document identifies the City’s 10-year capital needs and priorities for growth projects and investment targets for renewal based upon known funding sources, and the City’s financial capacity and debt position. This is considered in the context of strategic direction from City Council, alignment to corporate outcomes, external factors impacting the organization, the local and broader economic outlook are current and emerging trends driving the City’s business.

<u>Edmonton’s Economic Outlook</u>

Across Canada, longer-term employment growth is expected to slow as the impacts of an aging workforce are felt. Edmonton, with a relatively young demographic, will outperform Canada and continue to attract net migration given expected, continued growth. Consequently, the City will have to continue to address growth in population related service and structure requirements, while balancing infrastructure investment to serve the needs of its own, expanding senior demographic.

Overall, increased inflationary pressures are forecast for the period to 2024. After a strong anticipated movement upwards in 2014, the Non-Residential Construction Price Index is expected to sharply decelerate to about one per cent over the period from 2016 to 2018 as large energy related construction projects and public sector projects such as public education facilities and the Anthony Henday Drive are completed. This trend, however, could be reversed given the recent commitment to the Edmonton’s Valley Line

LRT Stage 1. In terms of City Capital impacts, however, real economic growth is expected to average 3.4% per cent. Basic project related costs experienced by the city can be expected to rise at or above 3 per cent on average as growth in labour and material costs impact Capital budgets. Interest rates beyond 2017 are expected to stabilize well above current rates, meaning the City should anticipate a long term upward trend in interest related expenses.

After very strong growth in 2012 and 2013, population in the City should expand at 2.1 percent per year to 2018. Beyond 2018, population growth will slow modestly, averaging about 2.0 percent per year out to 2024. This relatively modest growth in population will stabilize new home construction and, along with a return to more traditional mortgage costs, limiting the demand for housing units. As a result, while continuing to grow at modest levels, housing starts should average about 11,000 units per year from 2015 to 2024. Growth in suburban areas will continue to place pressure on certain forms of capital infrastructure - namely major road projects (interchanges and freeway improvements), new parks, fire halls, and growth in the transit fleet all with a goal to provide new and enhanced pubic services.

Edmonton's Economic Forecast is provided in more detail in Attachment 1.

Funding and Debt

The 2012–2014 capital budget was $2.94 billion, $979 million per year, for infrastructure spending. An additional $0.6 billion in carry-forward projects from the 2009-2011 cycle, and minor adjustments through supplemental capital budget adjustments placed planned spending at over $3.6 billion during the three year period. This level of funding was made possible through a combination of fast-tracking Grant eligible projects and use of tax supported debt in a strategic way for a number of key city building projects.

As the City enters the next 10 years, it will continue to use a combination of key Provincial Grant programs such as GreenTRIP and the Federal Building Canada Fund together with debt financing for advancing transformational projects such as the expansion of Edmonton's Light Rail Transit Network. Provincial Grants will be primarily comprised of Green TRIP, the Municipal Sustainability Initiative (MSI) and the Basic Municipal Transportation Grant (BMTG) - formerly Provincial Fuel Tax Grant. Federal Grants include the Building Canada Fund (BCF) and the Federal Gas Tax and all totaled, these grants will make up 37% of all capital budget revenue sources.

The other portion of revenues are city funded and will consist of sources such as the neighbourhood tax levy, local improvement funding, community/partner funding, reserves, and pay-as-you-go (PAYG) which include transfers from operating (Fleet, Police, Libraries, and Traffic Safety).

The total funding over the 2015-2018 period is projected to be $3.35 billion. Of this amount, more than one third ($1.34 billion) has already been allocated through prior Council decisions. Funding available for Council's allocation over the 2015-2018 period is $2.01 billion or $500 million per year. Figure 1 and 2 in Attachment 2 provide additional information on funding availability, and shows both historical and projected capital expenditures. Over the past 5 years, despite record funding levels, actual tax supported capital construction spending has averaged $892 million per year with a considerable amount of budget carry-forward each year. Assuming that the Edmonton construction market has capacity to deliver in the order of $1 billion in City capital projects, and taking the projected capital carry-forward from the 2012-2014 Capital Priorities Plan into account, Edmonton will continue to experience construction activity at a level similar to what was witnessed over the past 5 years.

The City's Debt Management Fiscal Policy (DMFP) guides civic borrowing through financial procedures and controls for the issuance and use of new debt to support the City's ability to meet current and future infrastructure challenges, while maintaining a favourable financial position. The Debt Management Fiscal Policy also clearly sets out that long-term debt related to capital expenditures can only be used for:

- Large projects with long-term benefits;
- Projects with benefits for the community-at-large (for tax-supported debt);
- Growth-related projects;
- Emerging needs to support corporate priorities and approved strategic plans; and
- Major rehabilitation of existing assets.

By the end of 2014, the City's total debt (tax supported and self liquidating) is estimated to total $3.56 billion. Once the Valley Line LRT is operational in 2020 the total debt level will increase to $4.04 billion and in 2015 the City will make its closest approach to the debt servicing limits outlined in the Debt Management Fiscal Policy. As City revenues increase so do the debt limits creating added debt room. City Revenues are predicted to be $2.6 billion in 2015 and rise to $3.8 billion in 2024, increasing annually by 4.9% over the 10 year period.

Figures 3 and 4 in Attachment 2 provide an overview of the projection of City debt and debt servicing over the 2015 to 2024 period.

Infrastructure Renewal

The 2012 - 2014 budget illustrated the City's sustained, strong commitment to maintaining its investment in renewal projects. A greater percentage of the total funding, 41 per cent, was directed to maintenance, compared to 34 percent in the 2009 to 2011 Capital Budget. This percentage reflects the increased, sustainable renewal investment underlined by the Neighbourhood Renewal Program.

Renewal projects focus on maximizing the effective utility of existing capital assets. Prioritizing renewal projects is achieved through a customized assessment methodology known as the Risk-based Infrastructure Management System (RIMS). Risk-based Infrastructure Management System provides a comprehensive understanding of the nature, scope and state of assets owned and maintained by the

City and provides an overview of the level of investment required to bring the inventory to a state and condition that is acceptable to Council and the citizens of Edmonton. Attachment 3 provides an overview of the City's asset management process including a summary of the individual asset categories.

The Risk-based Infrastructure Management System model recommends an annual reinvestment of $466 million (2013 dollars) from 2015-2018 and an average annual reinvestment of $607 million (2013 dollars) from 2019 to 2024 for tax supported assets. This figure does not include utility funded assets such as drainage and solid waste. Transportation related assets excluding buses require the highest renewal investment of an average of $234 million per year over the first four years, increasing to $387 million per year for the remaining six years. The next largest renewal need over the 2015-2018 time frame were Building assets at $78 million per year followed by $73 million per year for Fleet assets (including buses).

In addition to calculating recommended investment, Risk-based Infrastructure Management System can determine the impact of investing less than the recommended budget and the resulting affect on the percentage of City assets in Poor (D) and Very Poor (F) condition. The longer the required renewal of municipal assets is deferred, the more deterioration impacts are felt and the more expensive it becomes to bring these assets back to an acceptable condition. Chronic underfunding will create a backlog of deferred capital projects and drive costs up over the long-term. To demonstrate the impact of reallocating renewal dollars, two scenarios (reducing annual investment by $50 and $150 million dollars) were modeled. The results of this modeling, contrasted with the affect of the recommended investment, is provided in Attachment 3. Because the overall aggregate life span of the City's infrastructure is 45 years, the impacts of funding shortfalls or deficiencies may not be apparent immediately.

Building a Great City

As Edmonton grows, citizens will expect to be provided with infrastructure and services consistent with a modern and progressive city. Even with Council's residential infill target of 25%, and progressive infill options like the Blatchford redevelopment, the majority of population growth will occur in the suburban areas, primarily outside of the Anthony Henday Drive.

Not all growth investment requirements are the same. Council's strategic context, distribution of growth pressures, and changing demographics, all contribute to a policy environment through which highly complex investment decisions must be made. In preparing the 2015-2024 Capital Investment Agenda, Administration identified approximately $10 billion in potential growth projects. Since the Capital Investment Agenda is a long term planning document it is important to understand that, at this point in time, these projects have not all had business cases developed nor been prioritized or reconciled with available funding.

To aide in the understanding of the potential Growth needs under consideration over the span of the Agenda, growth projects were placed into the following categories:

1) Transformational - Major projects like LRT, Arena, Quarters, Blatchford.
2) New Investment - Infrastructure required to leverage further increases or diversification to the tax base. This would mainly be projects to support growth in new and developing Neighbourhood Structure Plan (NSP) areas like interchange enhancements on the Anthony Henday, District parks, as well and new industrial investment opportunities such as the Edmonton Energy and Technology Park.
3) Existing Reinvestment - Infrastructure to address functionality or downstream impacts of growth. This would be projects like facility additions to address functionality or capacity issues, improvements to the inner ring road (Yellowhead Trail, Whitemud Drive, 75 Street), park redevelopment or road safety and capacity improvements in existing areas.
4) City Operations - Infrastructure to support city operations. This would include transit garages, fleet, operating yards, and most of Information Technology.
5) External - Funding requests by outside agencies.

Attachment 4 provides an overview of the growth component of the Capital Investment Agenda.

Growth needs and priorities are initially identified at the department level, with recommendations put forward based on alignment to the The Ways, pre-existing Council commitments and an initial presumption of unconstrained funding. Presenting the City's growth requirements through a broad lens gives Council perspective on the full magnitude of need. From this vantage point, Council can articulate expectations and provide direction on priorities for growth investment over a 10-year horizon. Based on this direction, Administration then shapes the four-year capital budget, which will be presented to Council later in the year.

With respect to City Operations, Information Technology (IT) investment is one of many internal investments required for the growth and renewal of the City's capital projects. Technology is key in driving innovation; as such, effective use of technology can modernize an organization and transform service delivery. Although Information Technology projects make up a small portion of City capital budgets (1.6% in 2012-14), these investments are essential to deliver on the City's commitments.

The City is changing the way we invest in new Information Technology projects by improving governance, prioritization and decision-making processes for Information Technology investments. The framework will ensure that Information Technology projects are not competing or conflicting with other capital projects, and that funding is allocated in a responsible manner. This will allow Administration to reduce duplication, get the best value from investments and explore new opportunities to modernize and transform service delivery. The 2015-2018 Capital Plan will likely include a recommendation to set aside a block of funding for technology based investment.

Developing the 2015-2018 Capital Budget

Although Council must ultimately decide the extent to which they invest in each growth category, Administration has developed a framework to help prioritize its capital recommendations to Council. Seven primary criteria and three sub-criteria have been established as a framework to form a multi-criteria scoring process. In turn, each criteria will be weighted to determine the relative importance for each of the criteria. The prioritization score and listing in itself will not form the basis of Administration's recommendations to City Council. Project ranking will be further scrutinized on the basis of timing and synergies with other projects, relevance to current issues, available funding, and external factors.

The criteria are as follows:
- Mandate (Legislated, prior Council direction, etc.)
- Geographic Impact (for public facing projects) OR Organizational Impact (for internal support projects)
- Value for Money, which includes the following sub-criteria:
    - Anticipated Change in Demand (over and above average growth)
    - Capital or Operational Savings
    - Level of Service benefits
- Project Readiness
- Ability to supplement a renewal project
- Strategic Alignment with Council's Corporate Outcomes
- Ability to address Operational Risk

Attachment 5 provides a more detailed description of these criteria and the prioritization process.

The April 30, 2014, City Council session and the completion of the 2015-2014 Capital Investment Agenda will provide key direction in the formulation of the 2015-2018 Capital Prioirty Plan. Council direction with respect to the level of renewal funding, concurrence with the prioritization criteria and amount of funding allocated to roadway renewal for the Administration to continue to develop the draft 2015-2018 Capital Priority Plan.

Over the next six weeks, Administration will be meeting with the Mayor and each Councillor individually to allow members of Council to provide their perspectives into the Capital Investment Agenda and to understand the types of projects that will be advanced through the 2015-2018 Capital Priorities Plan process.

Policy

The Way We Finance
Debt Management Fiscal Policy

Corporate Outcomes

The Capital Investment Agenda supports all the Corporate Outcomes in *The Way Ahead*.

Justification of Recommendation

1) Fully funding Renewal to the recommended level outlined by the Risk-based Infrastructure Management System model results in the least risk from an asset management perspective. Deviating from the recommended renewal funding target will increase the amount of deferred maintenance, accelerate the deterioration of infrastructure and result in a greater funding requirement in the future.

2) The proposed Growth Project Prioritization Process is based on sound rationale and includes relevant criteria including alignment with *The Way Ahead*.

3) A funding level of $55 million per year for Arterial Renewal will be achieved by 2020 if Council desires to ensure that, on average, not more than 10% of the arterial roadway network is in need of rehabilitation.

Attachments

1. Edmontons Economic Outlook
2. 10-Year Capital Sources and Debt Forecast
3. Infrastructure Renewal
4. Building a Great City
5. Capital Growth Profile Prioritization