Funding Models for Fast Tracking LRT Construction

Recommendation:

1. That the City of Edmonton's share of financing for the West to South East LRT line, including the downtown connections, be subject to funding from other orders of government.
2. That the Mayor, on behalf of Council, have further discussions with other orders of government to obtain financial commitment towards new LRT in Edmonton.
3. The City of Edmonton's funding share of one-third be comprised of the following financing sources:
   a) Reallocation of Transportation growth projects financing of $200 million
   b) Tax supported debt
4. That the City debt servicing costs be financed through a combination of:
   a) An annual 0.5% tax increase for seven years commencing in 2012
   b) Fuel tax revenues
   c) Potentially a dedicated transit ticket LRT construction fare surcharge.

Report Summary

This report outlines for City Council key decision points and financing options to fast track LRT.

Previous Council/Committee Action

- At the January 19, 2011, City Council meeting, the following motion was passed:

  That the December 10, 2010, Finance and Treasury Department report 2010FTF036, be referred to the January 25, 2011, Transportation and Public Works Committee meeting to be dealt with as the second item of business, and that the Committee hear from speakers.

- At the December 10, 2010, City Council meeting, the December 10, 2010, Finance and Treasury Department report 2010FTF036 was postponed to the January 19, 2011, City Council meeting.
- At the May 4, 2010, Transportation and Public Works Committee meeting, the following motion was passed:

  That Administration provide a report to the June 29, 2010, Transportation and Public Works Committee meeting, on funding models for fast tracking LRT construction (NAIT, Southeast and West) based on Attachment 1 of the April 15, 2010, Transportation Department report 2010TD2385, including a detailed analysis of options and implications of no net tax levy increase.

Report

This project represents a significant shift in the way we manage the growth of our City, by aligning decisions with Council's 30-year vision and the 10-year goals for Transforming Edmonton. The City has limited resources to fund growth, forcing us to make trade-offs on what we can fund. Administration is recommending decisions on how to use the City's limited resources to advance three main goals: shifting transportation modes, transforming urban form, and preserving our environment. This means we would have to defer major growth projects, such as the building or widening of arterial roads, in favour of transit projects that reduce commuting in single-occupant personal vehicles.

Overview

The construction cost of the West to South East LRT line including the downtown connections is estimated at $3.2 billion using a design build construction delivery method and constructing by 2016. The cost is an inflated value based on expected construction cash flow. A private public partnership (P3) delivery method business case has also been prepared and the results of that will be presented to Council by Capital Construction in a January 2011 report. If applied to the West to South East LRT line as a whole, indication is that a P3 could offer some efficiencies that could reduce cost.

The total estimated cost of LRT expansion is $3.9 billion which includes $725 million for NAIT and $3.2 billion for South East, West, and the Downtown Connector (Attachment 1). In order to advance the project, the City would finance their one-third share of the total project costs, and require the balance from the other two orders of government.

To date, the province announced the terms and conditions of the $2 billion Green Trip program in mid 2010. The funding available to Edmonton and the Capital Region is $800 million. This announcement moves the City another step closer to advancing the fast tracking of LRT, and more immediately the completion of the $725 million NAIT Line which Council approved subject to Green Trip funding. The Capital Region Board has endorsed the application of $732 million in Green Trip funding for LRT construction in order to advance the Board's vision of a more transit-friendly Capital Region.

The federal government is expected to contribute $75 million for the NAIT line using the Building Canada Fund.

As noted previously, the full $3.9 billion for LRT expansion for the South East, West, Downtown Connector and NAIT needs to be cost shared with the federal and provincial governments in order for the full expansion to proceed. The funding for the NAIT phase of the expansion has not been equally shared between the three orders of government; therefore, the remaining fund sharing should see a greater share from the federal government to achieve equal contributions overall.

In the absence of a commitment for equal federal funding, a case should be made to the Province to take on a greater share of the cost. The City does not have the fiscal capacity to fund more than $1 billion of the total cost of the project unless there is more direct tax support.

What can the City afford

The 2012-2018 funded Capital Plan totals $4.7 billion, of which $1.7 billion is for growth projects and $3 billion is for rehabilitation projects (Attachment 2).

In addition to the funded plan there are several large unfunded emergent projects including the Walterdale Bridge, the Rossdale/EPCOR decommissioned power plant building redevelopment, Northeast Anthony Henday Drive connectors and the Quarters.

Deferral of growth projects

Of the $1.7 billion in funding for growth projects, only $438 million could potentially be reallocated to fund LRT. Funding for projects that have either been committed, started, or are financed from another source, cannot be reallocated to LRT.

Out of the $438 million, Administration has identified $200 million in funding for Transportation growth related projects that could potentially be available through project deferrals (see Attachment 3).

Reallocation of rehabilitation projects

Of the $3 billion in funded rehabilitation projects, $1.4 billion is dedicated to the Neighbourhood Renewal Program. As a key Council priority, dollars earmarked for the Neighbourhood Renewal Program were not considered for reallocation.

Of the remaining $1.6 billion, $1.4 billion could potentially be reallocated. Given that rehabilitation is already $4.5 billion (59 percent) underfunded for the years 2012-2018, Administration does not recommend reallocation of funding for rehabilitation projects; any dollars removed from rehabilitation will increase the City's infrastructure backlog.

This assumption is reinforced by the City's risk assessment modeling that shows the City needs to invest 1.7 percent of its asset replacement value each year to maintain its asset base. In 2009, the replacement value of the City's infrastructure assets was $37 billion, which based on the model requires an investment of $625 million each year for rehabilitation. The City's current level of investment is about $457 million. Though the City has been increasing its investment in rehabilitation with programs such as Municipal Sustainability Initiative and the Neighbourhood Renewal Program, we are still falling short by $168 million per year.

While current investment is a step in the right direction, it is only beginning to address the backlog, and it will take years before we begin to maintain our infrastructure at an acceptable level of performance and risk.
See Attachment 4 for more detail on rehabilitation projects.

Debt and Debt Financing

The amount of City debt is governed by limits imposed through the *Municipal Government Act*, and further restricted through Council's approved Debt Management Fiscal Policy. The most restrictive limit is the total debt limit, which is double the amount of annual eligible City revenues.

Debt has only been re-introduced for tax-supported operations since 2002. Since 2008, the City has substantially increased the investment in City infrastructure with debt financing contributing to that re-investment (e.g. Great Neighbourhoods Initiative, SLRT, NLRT, refurbishment and widening of the Quesnell Bridge, new recreation centres).

In 2010, $0.6 billion of debt room remains. By 2012, $1 billion is projected to be available. The debt room increases as the City's eligible revenue streams grow. Any decision on debt allocation for LRT construction should allow for some flexibility to fund future projects.

Debt Servicing

Debt servicing payments require a dedicated ongoing revenue source. Looking at the City's revenue streams, fuel tax (currently available for principal payments only), potential transit ticket LRT construction surcharge and tax revenues could be used.

For more detail on funding options to service debt, see Attachment 5.

Financing Implications

The timing of the cash availability from Municipal Sustainability Initiative, provincial fuel tax and pay as you go impacts the financing of this project to a significant degree.

Both Municipal Sustainability Initiative and fuel tax have been fast tracked for other transportation projects to take advantage of economic conditions. This project fast tracking removes any flexibility of transferring financing from these committed projects to the LRT project.

There has also been a reduction in the cash flow from the province with respect to Municipal Sustainability Initiative which has impacted financing of projects.

The financing options are all predicated on construction completion by 2016. An extension to the construction schedule would reduce the annual debt servicing requirement in the short run.

Funding Scenarios

Based on the City's need to fund $1.3 billion to fund LRT expansion (including NAIT), two financing scenarios are summarized below.

The scenarios are based on a total funding requirement of $1 billion as the City has already approved $305 million through funding approvals for NAIT that can be utilized for further LRT expansion (Attachment 6).

1. Growth Reallocation Scenario

This scenario proposes reallocating $200 million from transportation growth projects, and approximately $800 million in debt financing. The debt would be serviced through fuel tax. Debt repayment would be $56 million per year over a 25-year term.

Based on the current fuel tax funding within Transportation, the reallocation of $56 million in fuel tax would represent a significant deferral of transportation rehabilitation programs including bridges, replacement buses, and arterial roads. The reallocation for 2012-2018 would represent over two thirds of the fuel tax available as fuel tax expenditures have been fast tracked in the 2009-2011 capital budget. Beyond 2018, this level of fuel tax for debt servicing would leave less than half for other transportation growth and rehabilitation projects.

An allocation of $56 million from fuel tax would remove this as a funding source for rehabilitation projects which would add to the infrastructure deficit. The fuel tax allocation could be partially substituted with other revenue sources such as a transit ticket LRT construction fare surcharge.

2. **Growth Reallocation/Tax Levy Scenario**

This scenario also proposes reallocating $200 million from transportation growth projects but puts forward both fuel tax and tax levy to service the debt. This scenario requires approximately $800 million in debt financing with repayment being $56 million per year over a 25-year term. This could be serviced with $19 million of fuel tax and $37 million of tax levy. The tax levy impact can be mitigated by phasing the increase over a seven year period by a 0.5% annual increase.

The debt servicing impact could be reduced by $7 million to $16 million, if Council chose to reallocate debt from approved but not yet started tax-supported debt projects such as the Meadows Recreation Centre and years 2012-2018 of the Great Neighbourhoods Program.

More detail on the scenarios is provided in Attachment 6 including a combined rehabilitation and growth reallocation scenario.

Life Cycle Costs

The expanded LRT would require significant rehabilitation investment costs over the life of the asset that would include light rail vehicles, facilities, and electrical and communication equipment. The estimated life cycle costs are considered in the business case analysis to be reported by Capital Construction Department in January.

Operating Costs

The operating costs for the expanded LRT are expected to be $17 million annually. The operating costs that would be removed from the existing transit operations that are serviced by buses are estimated to be $10 million. The operating cost impact would be partially offset by increased revenue due to higher transit system ridership.

Policy

- Council Policy 203C, Debt Management Fiscal Policy provides direction on the application of borrowing. The report recommendations are consistent with the Policy.
- LRT planning and construction aligns with the goals and objectives identified in The Way We Move and The Way We Grow including increasing transit ridership, transit mode split, and to spur the development of compact, urban communities.

Focus Areas

LRT planning and construction aligns with the City's 10-year strategic goals of shifting its transportation mode and transforming Edmonton's urban form.

Justification of Recommendation

1. The City does not have the fiscal capacity to fund the LRT expansion on its own. Support from other orders of government is needed.
2. Commitments from other orders of government are required in order for the project to proceed. While progress has been made in obtaining some funding from the other orders of government, further discussions are required if a 2016 completion date is to be achieved.
3. Given the significant cost of LRT expansion over a relatively compressed time frame, a combination of deferring some growth-related transportation projects and use of new tax-supported debt is recommended. Rehabilitation projects were not recommended for reallocation, given the potential longer term impacts. From a financial perspective postponing rehabilitation creates backlogs and leads to higher replacement costs. From a condition and risk perspective, postponing rehabilitation results in assets deteriorating further during the deferral period.
4. Debt servicing requires an ongoing stable funding source with fuel tax and tax levy being the best alternatives. In the absence of a tax levy increase a significant portion of provincial fuel tax would need to be redirected to servicing debt which would then have long term impacts on rehabilitation and growth projects.

Attachments

1. Schedule of LRT Costs and Funding
2. Current Capital Plan and Financing
3. Capital Plan Summary – Growth Projects
4. Capital Plan Summary – Rehabilitation Projects
5. Debt Limits and Debt Servicing Options
6. Scenarios for LRT Fast Tracking

Others Reviewing this Report

Corporate Leadership Team

Schedule of LRT Costs and Funding

Summary of Costs

	Approved	Proposed[1]					Overall Totals	
	NLRT	SELRT	WLRT	Downtown Connector	Subtotal	%	$	%
City	170	634	441	65	1,141	36%	1,311	33%
Provincial	480	462	321	47	831	26%	1,311	33%
Federal	75	687	478	71	1,236	39%	1,311	33%
Total	725	1,783	1,241	183	3,207	100%	3,932	100%

Summary of Funding

	Approved and Committed Funding			Additional Funding Required	Overall Totals	
	NLRT	Other Lines	Subtotal		$	%
City	170	135	305	1,006	1,311	33%
Provincial[2]	480	212	692	619	1,311	33%
Federal	75	-	75	1,236	1,311	33%
Total	725	347	1,072	2,860	3,932	100%

1. Proposed LRT costing includes inflation over expected construction timelines.
2. Capital Region Board approval for Green Trip represents $692 m for NAIT SE to West lines and $40 m for regional LRT.

Current Capital Plan and Financing

2008-2017 Preliminary Capital Investment Agenda

The City's 2008-2017 Preliminary 10-Year Capital Investment Agenda identified $27.2 billion of required capital investment for growth ($16.2 billion) and renewal ($11 billion) during the plan's timeframe. At the time, sources of funding totalled $8.1 billion, which included $2 billion of MSI. This translated to an infrastructure shortfall of $19.1 billion, or about 70 per cent of the total estimated need.

The Capital Investment Agenda also incorporated a number of capital direction setting principles that Council approved in April 2008. These financial and infrastructure principles are intended to direct capital planning and to guide Council in their investment decisions.

These key principles included:

- Using cash for ongoing projects (i.e., maintenance and renewal);
- Using borrowing for new and large projects;
- Maintaining what is built;
- Using rehabilitation funding to ensure that assets meet acceptable standards;
- Only building if the life cycle costs are affordable.

2012-2018 Capital Plan

With the approval of the 2009-2011 Capital Budget, the 10-year Capital Investment Agenda was updated to extend to 2018. The update also took into account the cost de-escalations that occurred with the recent economic downturn.

An assumption has been made that no dollars from the approved 2009-2011 Capital Budget will be reallocated to LRT. Therefore, any reallocation of capital dollars will need to come from the 2012-2018 Capital Plan, which already includes a funding shortfall of $8.5 billion –$4 billion in growth and $4.5 billion in rehabilitation.

Although the 2009-2018 Capital plan includes 43% growth projects and 57% rehabilitation projects overall, growth projects formed a larger share of the 2009-2011 Approved Capital Budget meaning the balance of the capital plan from 2012-2018 is more heavily weighted towards rehabilitation projects (36% growth and 64% rehabilitation). Ultimately, there is a smaller share of growth projects in the 2012-2018 Capital Plan available for reallocation.

Emerging Projects and Initiatives

A number of emerging projects and initiatives on the horizon that are unfunded and not reflected in the current Capital Plan could add to this $8.5 billion shortfall. These include (approximate costs):

- Walterdale Bridge (re-build) – $100 million
- West Rossdale/EPCOR buildings redevelopment – $200 million
- Northeast Anthony Henday connectors – $60 million
- The Quarters – up to $200 million

Financing Sources

The 2012-2018 Funded Capital Plan, summarized in the table below, includes $1.7B of growth related projects, $1.4B of neighbourhood renewal projects as well as $1.6B of other rehabilitation projects for a total of $4.7B over the 7 years.

2012 – 2018 Capital Plan by Financing Source ($Millions)

Financing Source	Growth	Rehabilitation		Total
		Neighbourhoods	Other Assets	
Funding Approved for LRT:				
Green Trip – LRT (Note 1)	270	-	-	270
Tax Supported Debt	58	-	-	58
MSI for NLRT	60	-	-	60
Total Funding Approved for LRT	**388**	**-**	**-**	**388**
Not Available Funding Sources:				
2% - Neighbourhoods	-	892	-	892
Tax Supported Debt	166	105	27	298
Retained Earnings	475	-	77	552
Local Improvements	35	25	10	70
Developer Financing	46	-	42	88
New Deal Public Transit	-	-	11	11
Other	139	0	12	151
Total of Not Available Sources	**861**	**1,023**	**178**	**2,062**
Available for Reallocation to LRT:				
Fuel Tax	137	-	466	603
Pay as You Go (formerly General Financing)	83	121	439	643
MSI (other than for NLRT)	218	273	538	1,029
Total of Available Funding Sources	**438**	**393**	**1,444**	**2,275**
Grand Total	**1,687**	**1,416**	**1,622**	**4,725**

Notes:
1) $150M of Green Trip is budgeted for 2011, leaving the balance of $270M from 2012- 2018. This does not consider recent recommendations of the Capital Region Board on Green Trip allocation to LRT.

Within the 2012-2018 Capital Plan, the sources of funding that could be reallocated to the LRT are:

1. Provincial Fuel Tax (also called City Transportation Fund or CTF)

Established in 2000, the fuel tax provides funding to Edmonton and Calgary for capital transportation projects within the two cities. Eligible projects are focused primarily on primary highways and major streets through the cities, and major public transportation system requirements.

The grant is based on five cents per litre for the volume of road-use gasoline and diesel fuel delivered to service stations and bulk fuel outlets within each of the two cities. The grant program replaced all other transportation grants for Edmonton and Calgary. The City received $107.6 million in 2009-2010. Following a recent Provincial audit and review of the allocation method behind Fuel Tax, the City is now expected to receive from $98-105 million annually from the years 2012-2018.

The City made the decision for 2009-2011 to fast track projects by borrowing $100 million against future fuel tax payments. This fast tracking strategy requires repayment of $22 million including interest per year for 5 years. This reduces the amount of fuel tax available for reallocation over the next five years.

The fuel tax currently funds a variety of roads and transit projects. As a predictable and sustainable source of revenue that varies with the volume of fuel delivered, it is a viable financing source for reallocation to LRT. Diverting these dollars, however, means taking money away from transportation growth and rehabilitation projects, which will ultimately require these projects to be postponed, or reprioritized.

2. “Pay-As-You-Go” Financing

As of 2010, “pay-as-you-go” financing (formerly referred to as General Financing) is no longer tied to the tax levy, but rather to investment earnings, EPCOR Gold Bar transfer fees, and the ED TEL Endowment Fund dividends. The return on these investments, though still part of the operating budget are now used to fund capital, thereby insulating the operating budget from the volatility of these funding sources.

The current capital plan (2012-2018) identifies $643 million of “pay-as-you-go” financing; however, only $426 million is projected to be available over the next seven years. This is based on current earning estimates and also factors in payments that are required to pay down the shortfall created in the 2009-2011 operating budget when “pay-as-you-go” was linked to investment earnings.

$121 million of “pay-as-you-go” is allocated to the Neighbourhood Renewal Program. Most of the remaining $342 million in “pay-as-you-go” is required for the following purposes:

- to fund grant matching requirements;
- to fund ineligible costs; and,
- to fund projects that do not qualify for grants.

For example, MSI funded projects alone, require up to $108 million of "pay-as-you-go" to cover ineligible costs during the 2012-2018 period.

3. MSI (Municipal Sustainability Initiative)

The current Capital Plan (2012-2018) includes $1.1 billion of MSI. Edmonton received $91.8 million in 2008-2009 and was to receive $111.1 million in 2009-2010, ramping up to $260.7 million annually in 2010-2011.

MSI revenues, however, are lower than anticipated. The City saw a $40 million reduction in 2009 and a $100 million reduction in 2010 from what was originally committed. In addition, new MSI guidelines introduced in 2009 imposed a $1 million threshold for project eligibility, which deemed $15.6 million of City projects (i.e. parks playgrounds, library renewal) ineligible, and therefore requiring other funding sources.

The City committed to fast track about $260 million of MSI projects in 2009-2011 to bridge the gap between construction and receipt of funding. This fast tracking strategy requires repayment of $57 million including interest per year. This reduces the amount of MSI available for reallocation over the next five years.

Other commitments for MSI include $273 million for the Neighbourhood Renewal Program and $60 million for the NAIT Line.

While MSI dollars identified in the current Capital Plan (2012-2018) are committed, reallocation of MSI dollars to LRT (beyond the $60 million earmarked for the NAIT Line) remains an option for City Council.

Diverting these dollars, however, will mean taking money away from growth and rehabilitation projects that have already been allocated for MSI funding. The City allocated MSI funding based on the Council-approved split of 60 per cent to renewal and 40 per cent to growth, as well as the application of decision-making tools and criteria which selected the projects based on need, priority and corporate strategic direction.

Capital Plan Summary – Growth Projects

2012-2018 Capital Plan – Growth Projects Only ($ Millions)	2012-2018 Capital Plan
All Funding Sources	**1,687**
Funding Approved for LRT:	
Green Trip	270
MSI	60
Tax Supported Debt	58
Total Funding Approved for LRT	**388**
Not Available Funding Sources:	
Tax Supported Debt (Meadows)	137
Tax Supported Debt (Other)	29
Land Fund Retained Earnings	475
Local Improvements	35
Developer Financing	46
Other (e.g. Reserves)	139
Total Not Available Funding Sources	**861**
Available Funding Sources	
Transportation:	
Streetscape	16
Bus Facilities and Equipment Growth	13
Snow Storage Facilities Development	17
Operating Yards and Facilities	83
Arterial Network Improvements	87
Inner Ring Loop and Highway Connectors	51
Transit Vehicle Growth	33
Other Transportation	43
Total Transportation	343
Other Departments:	
Police Stations	26
Fire Stations	12
Parks	36
Recreation Centres and Libraries	21
Total Other Departments	**95**
Total Available Funding Sources	**438**
Growth Projects Recommended Reallocation	
Total Growth Projects	438
Less: Transportation Growth Projects Recommended for Reallocation	(200)
Growth Projects remaining in 2012 – 2018 Capital Plan	**238**

Transportation Growth Projects for Reallocation to LRT:

Project #	Project Name	2012-2018 Capital Plan
09-66-1070	SW Satellite Yard	10
09-66-1440	50 Street Widening (Whitemud to Roper)	13
	50 Street Widening (76 Avenue – 90 Avenue)	23
	50 Street Underpass CPR Track	13
	Noise Wall	4
	ITS	3
	Final Pavement Overlays	14
		70
09-66-1480	41 Avenue – QE11 Contingency	40
	Whitemud Drive (34 Street – 66 Street) widen to 6 lanes	7
	Overlays	3
		50
09-66-1296	LRT Signal System Upgrad	14
09-66-1420	Transportation Computer System Expansion (DATS, etc.)	6
05-66-1665	Stony Plain Road (142 St – 149 St) Transit Priority Corridor	9
09-66-1681	New Bus Purchases (Approx 80 buses)	41
Total Transportation Growth Projects for Reallocation to LRT		**200**

Growth Projects Not Recommended for Reallocation

Project #	Project	2012-2018 Capital Plan
03-20-0019	Mill Woods Branch Relocation & Expansion	13
03-28-4147	Louise McKinney Riverfront Park	6
06-20-0002	Clareview Branch Library	3
07-21-5746	Artificial Playing Surfaces: Qdrnt Based	4
07-60-1356	South West Division Station	6
07-60-1375	Northwest Division Station	20
08-70-0023	Heritage Valley Fire Station Construct	5
09-28-1050	New Park Construction	15
09-28-7001	NPDP/Outdoor Aquatic Amenities – NEW	15
09-70-0022	Fire Stations – Master Plan Phase I	7
10-21-5784	Lewis Farms Multi-Purp Fac – Design	1
		95

Capital Plan Summary – Rehabilitation Projects

2012-2018 Capital Plan – Rehabilitation Projects Only ($ Millions)	2012-2018 Capital Plan
All Funding Sources	**3,038**
Less: Neighbourhood Renewal	(1,311)
Less: Great Neighbourhoods	(105)
Subtotal	1,622
Less: Not Available Funding Sources	
Tax Supported Debt	27
Land Fund Retained Earnings	77
Local Improvements	10
Developer Financing	42
Other	22
Total Not Available Financing Sources	**178**
Rehabilitation Projects Funded by Available Sources	**1,444**

Breakdown of Rehabilitation Projects Funded by Available Funding Sources

	2012-2018 Capital Plan
Non-Transportation Projects	
Building and Facilities Renewal	193
Corporate – Fleet	5
Corporate – Renewal of IT Infrastructure	88
Economic Development – Shaw Conference Centre	31
Parks – Utilities and Access	29
Parks – Parks Renewal	109
Protection – Renewal of Police IT Infrastructure	23
Protection – Police Facilities	9
Protection – Fire Rescue Equipment	4
Rec & Cultural – Libraries	24
Rec & Cultural – Renewal of IT Infrastructure	6
Rec & Cultural – Other	8
Total Non-Transportation Envelopes	**528**
Transportation Projects	
Roads – Bridge Rehabilitation	178
Roads – Arterial/Primary/Highway Renewal	295
Roads – Traffic Control and Safety	23
Roads – Streetlighting	53
Roads – Other	36
Transit – LRV Retrofit	4
Transit – Bus Fleet	59
Transit – Facilities	252
Transit – Safety and Security	15
Total Transportation Projects	**915**
Overall Total	**1,444**

Funding Required for Debt Incurred During Construction

In the 2012-2018 period, Transportation needs to defer $200 million in growth projects, and repay fast tracking of fuel tax and MSI from the 2009-2011 period. This leaves only rehabilitation projects to deal with any funding reallocated to debt servicing for LRT.

Even with funding scenarios where tax levy is used to fund long term debt, some amount of funding is required for debt servicing both long term and during construction. Provincial Fuel Tax has been recommended as a funding source for debt servicing during construction. The actual amounts required for debt servicing during the construction period will vary depending on the overall choices made for funding LRT.

The following table demonstrates the impact if $200 million of rehabilitation projects was deferred to help fund LRT. All options begin with $116 million required to provide debt servicing over the 2012-2018 period (a deferral of 13% of all transportation rehabilitation projects with available funding sources). On top of this reallocation, the options include transportation exclusively bearing the additional $200 million of deferred rehabilitation projects (deferral of 35% of transportation rehabilitation projects available), other departments only (deferral of 13% of transportation rehabilitation projects and 38% of other departments), or a shared deferral (total deferral of 22% across the board).

Impact of Debt Servicing Construction and $200M of Rehabilitation Deferral

	Transportation		**Other Departments**	
	$	**%**	**$**	**%**
Capital Plan Before Deferral	**915**		**528**	
Scenario 1: Transportation Only				
Debt Servicing Required during 2012-2018	(116)	-13%	-	0%
Transportation Rehabilitation Deferral	(200)	-22%	-	0%
After Transportation Only	**599**	**-35%**	**528**	**0%**
Scenario 2: Other Departments Only				
Debt Servicing Required during 2012-2018	(116)	-13%	-	0%
Other Departments Deferral	-	0%	(200)	-38%
After Other Departments Only	**799**	**-13%**	**328**	**-38%**
Scenario 3: Shared Deferral				
Debt Servicing Required during 2012-2018	(116)	-13%	-	0%
Shared Deferral (Pro-Rata)	(84)	-9%	(115)	-22%
After Shared Deferral across All Departments	715	-22%	413	-22%

Rehabilitation Challenges

Given that rehabilitation is already $4.5 billion (59 per cent) underfunded for the years 2012-2018, any dollars removed from rehabilitation will increase the City's infrastructure backlog.

This assumption is reinforced by the City's risk assessment modeling that shows the City needs to invest 1.7 per cent of its asset replacement value each year. In 2009, the replacement value of the City's infrastructure assets was $37 billion, which based on the model requires an investment of $625 million each year for rehabilitation. The City's current level of investment is about $457 million. While the City has been increasing its investment in rehabilitation with programs such as MSI and the Neighbourhood Renewal Program, we are still falling short by $168 million per year.

While current investment is a step in the right direction, it is only beginning to address the backlog, and it will take years before we begin to maintain our infrastructure at an acceptable level of performance and risk. Another consideration is that as we add to the asset inventory each year the City's investment in rehabilitation needs to increase. Therefore, removing dollars from rehabilitation will undermine our progress and will cost more in the long run.

Neighbourhood Renewal Program (NRP)

In the 2009 Budget City Council approved the earmarking of two per cent in property taxes each year for the three years 2009-2011 (to be reviewed and evaluated for subsequent years) to fix crumbling neighbourhoods. The premise of the program was to establish an ongoing sustainable fund for neighbourhood infrastructure renewal.

There are two project profiles for this program (09-66-1056 for the two per cent tax levy and 09-66-1055 for the program's other sources of funding, such as local improvements, "pay-as-you-go", AMIP and MSI).

With the approval of the two per cent earmarking and the recent cost de-escalations in the transportation sector, the City has been able to undertake additional NRP work, even though there have been some capacity challenges that have come with more favourable pricing. Although the favourable recent pricing for neighbourhood renewal work might suggest the reallocation of some of the funding for this program is possible, any reallocation could undermine the long term success of the neighbourhood renewal program. A review of the first 3 years of the Neighbourhood Renewal program will be completed in early 2011 and be used for development of the 2012-2014 Capital Budget.

While the NRP has demonstrated progress to date, the program is just beginning to tackle the neighbourhood infrastructure backlog. As of year-end 2009:

- 174 neighbourhoods required renewal:
    - 109 neighbourhoods required construction; and,
    - 65 neighbourhoods required overlay

In fact, the number of neighbourhoods requiring rehabilitation still continues to grow, because the program has not been in place long enough for the rate of rehabilitation to be greater than the rate or deterioration. Also, alleys, which are within the scope of the program, are still unfunded.

The project profile that includes “pay-as-you-go”, MSI and AMIP does not extend beyond 2018; as such, the program will need to be fully funded through the two per cent tax levy by that year. Until then, these funding sources are required to supplement the tax levy while the fund is building up to match program needs.

Given the NRP is only beginning to address the neighbourhood backlog and still requires many more years to build up a fund to meet the program’s life cycle objectives, reallocating any NRP dollars to LRT will reverse the progress made to date and ultimately cost the City more to catch up in the future.

Debt Limits and Debt Servicing Options

Debt Limits
When it comes to infrastructure, the immediacy of borrowing can be a significant advantage. Since debt-financing is a way to finance large expenditures up front, it allows high priority projects to proceed today as opposed to deferring them until enough "pay-as-you-go" funds are available.

Debt is a particularly favorable approach if it can also lever more capital dollars elsewhere, such as federal or provincial grants or participation from the private sector. There is also an advantage to using debt when the inflationary costs of a project are greater than the cost of borrowing and when capacity is available.

An appropriate and sustainable level of tax-supported debt is recognized as a legitimate part of any long-term capital financing plan. The key to utilizing this financing tool is to establish sustainable limits, ensure the debt is used for the right projects, as well as structured appropriately with a repayment plan in place.

The Municipal Government Act prevents municipalities from having debt exceed two times their revenues and debt servicing costs are not to exceed 35 per cent of their revenues.

Under the City's current borrowing policy, tax-supported debt servicing is limited to 15 per cent of tax revenues and total debt servicing to 22 per cent of revenues. Chart 1 forecasts the City's total debt limit and capacity. This is the most restrictive limit for the City.

After debt commitments, about $0.6 billion of total debt room is currently available under the MGA limits (18% of capacity). With projected growth in City revenues, the remaining debt room is expected to be about $1.0 billion in 2012 and will grow as City revenues grow and existing debt is paid down. A key assumption of the forecast is the level of revenue growth for the City.

Debt has only been re-introduced for tax-supported operations since 2002. Since 2008, the City has substantially increased the investment in City infrastructure with debt financing contributing to that re-investment (e.g. Great Neighbourhoods Initiative, SLRT, NLRT, major interchanges, new recreation centres).

Using a significant amount of our available debt room for one specific project in a short period of time could impact our ability to borrow for future high priority projects. Taking an aggressive borrowing approach may also impact external credit rating agencies view on the City's debt program and ultimately on the City's credit rating.

Additional debt room could be made available by reallocating an already approved tax-supported debt projects to LRT. The $105 million Great Neighbourhoods Initiative and the $137 million Meadows Recreation Centre and Library are the only two tax-supported debt projects that are potentially available for reallocation.

Debt Servicing Options

Chart 2 depicts the impact of the LRT financing scenarios on the City's debt servicing limits as per the MGA as well as the Debt Management Fiscal Policy (DMFP) Total Debt Servicing and Tax Supported Debt servicing limits. In all cases, the City remains within the policy and Provincial limits. Total debt servicing peaks at 13.2% of City revenues in 2016, while tax supported debt servicing peaks at 11.2% in 2016 based on $806 million in new borrowing for the LRT fast tracking.

Available ongoing financing options for debt servicing are:

1. Provincial Fuel Tax

If this grant program is used to service LRT debt, the dollars can only be used to repay the principal (not interest). This program guideline may be negotiable, as the province has allowed interest costs as an eligible expense under MSI.

The fuel tax is considered a viable source of revenue to service LRT debt. Reallocating these dollars, however, means taking money from transportation growth and/or rehabilitation projects for the term of the borrowing.

2. Transit Operating Savings

It is estimated that the new LRT lines will result in approximately $10 million in annual bus operating cost savings. These savings are more than offset by $17 million in increased operating costs for the new LRT system. The $7 million dollar net operating cost increase is expected to be partially offset by increased revenue due to higher transit system ridership. No dollars are expected to be available for allocation from transit operating. As such, this option cannot be viewed as an ongoing source of revenue to service long term debt.

3. Tax Levy

Currently, a one per cent increase in tax levy generates about $9 million.

As outlined in the growth reallocation/tax levy financing scenario below, a 0.5 per cent tax levy would generate about $4.5 million in year one and grow to $37 million in year seven (2012-18). At year seven, the $37 million could remain in the tax base to fund the debt servicing costs. Once the debt is paid, the $37 million in the tax base could be used for the LRT life cycle costs (i.e. to pay for the maintenance, rehabilitation and eventual replacement of the asset).
This option would see us collecting tax levy incrementally from 2012-2018 to pay for the debt as it is incurred during LRT construction from 2011-2016.

4. Transit LRT construction Fare Surcharge

A fare surcharge of $0.25 would generate up to $6 million per year which could be used to reduce the fuel tax requirement for the repayment of debt. This option requires more analysis before being recommended.

Chart 1: Total Debt vs. MGA Debt Limit

All Approved borrowing for tax-supported (includes NLRT & Great Neighbourhoods) as at Nov 2010
Includes Impact of Scenario 1-3 for LRT Fast Tracking

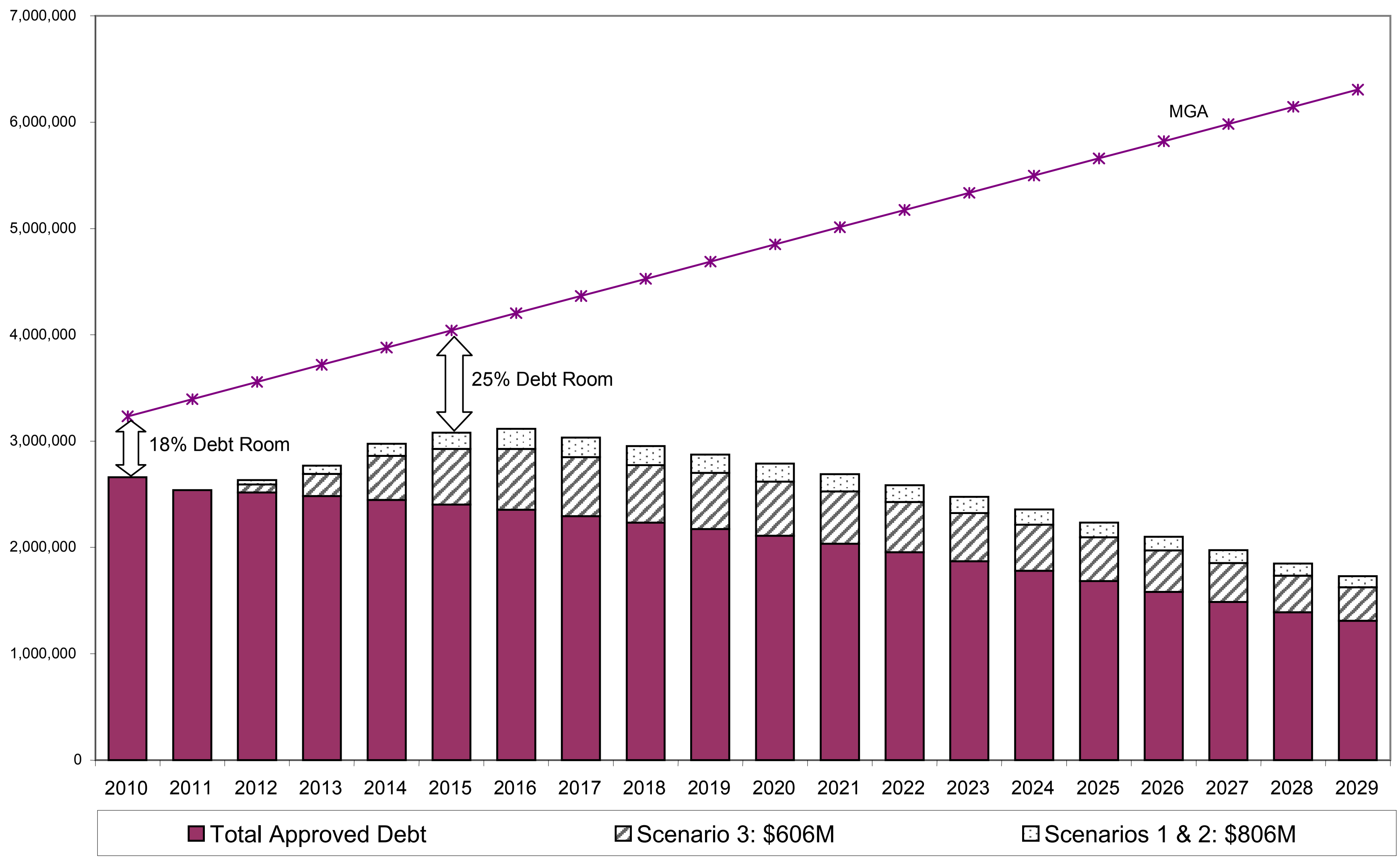
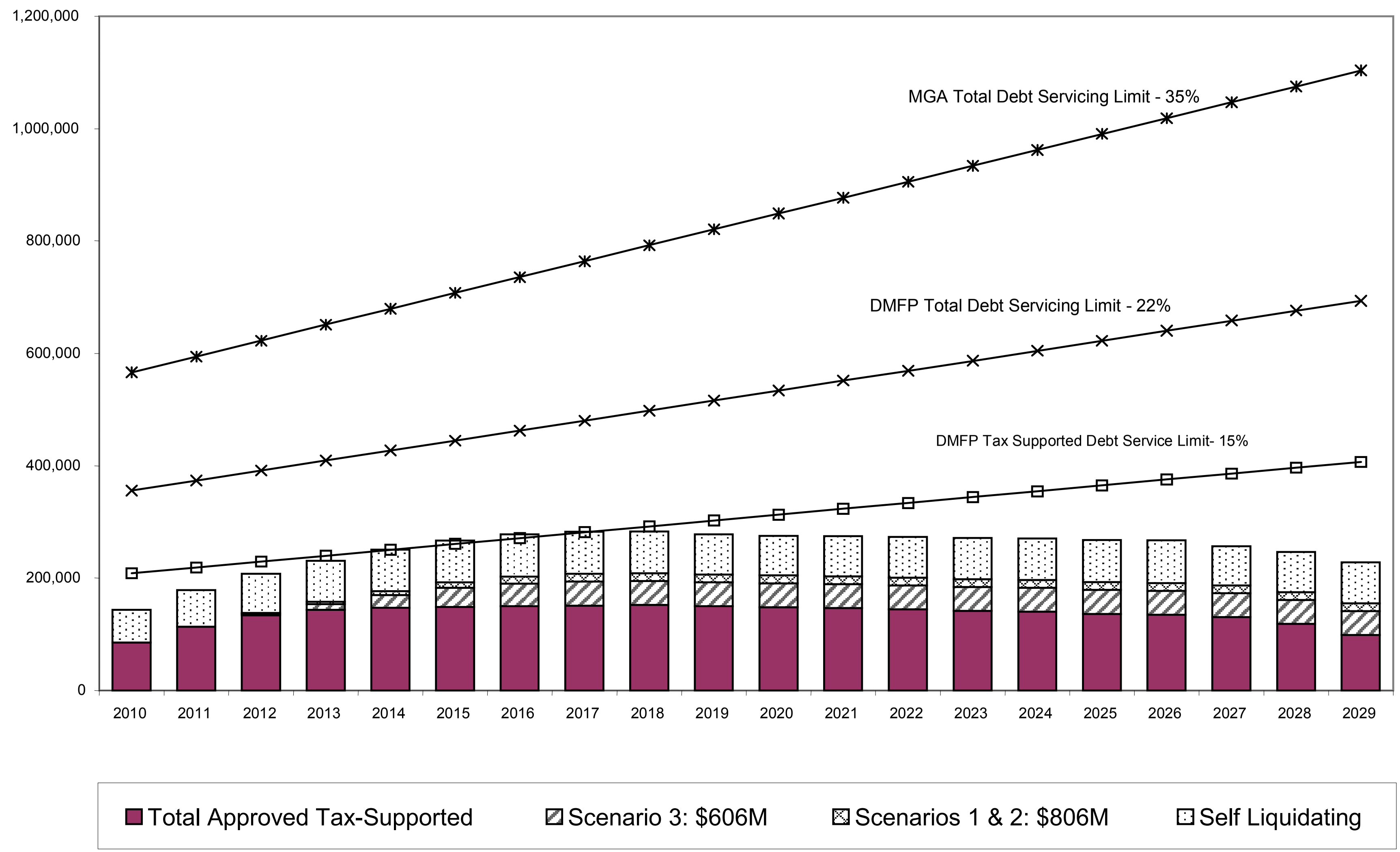


Chart 2: Debt Service Costs vs. MGA and Policy Limits

All Approved Borrowing for Tax-Supported (including NLRT & Great Neighbourhoods) as at November 2010
Includes Impact of Scenario 1-3 for LRT Fast Tracking



Scenarios for LRT Fast Tracking

Calculation of City's Share of LRT Fast Tracking	$ Millions
City's 1/3 Share of $3.932 billion	1,311
Less: approved NLRT City Funding	
Tax Supported Debt	(235)
MSI	(60)
LRT Reserve	(10)
Remaining Required Financing for City's Share	**1,006**

Financing Scenarios for Fast Tracking LRT	No Tax Levy Increase 1. Growth Reallocation	Tax Levy Increase 2. Growth Reallocation/ Taxy Levy	No Tax Levy Incrase 3. Growth/ Rehabilitation Reallocation
Project Financing			
Cash			
Growth Projects	200	200	200
Rehabilitation Projects	-	-	200
Total Reallocation (Cash)	**200**	**200**	**400**
Debt	**806**	**806**	**606**
Total City Share	**1,006**	**1,006**	**1,006**
Debt Servicing (Note 1)			
Provincial Fuel Tax	56	19	42
0.5% annual tax levy increase from 2012 – 2018	-	37	-
Total Debt Servicing (Note 2 and 3)	**56**	**56**	**42**
Total Interest Paid	594	594	444

Notes:
1) Based on 25 years at 4.736% (November 15, 2010 ACFA rate of 4.236% + .50% allowance).
2) Reallocating an existing approved tax supported debt project to LRT could reduce the Fuel Tax and/or tax levy required to serve the debt by $7 - $16 million annually.
3) A Transit LRT Construction Fare Surcharge of $0.25 would generate $6 million per year which could be used to reduce the fuel tax requirement for the repayment of debt.

Key Issues to Consider

Scenario 1: Growth Reallocation; No Tax Increase Scenario (not recommended)

This scenario requires a significant amount of debt ($806 million over 25 years) to be serviced solely with fuel tax dollars.

This would require $56 million of fuel tax each year for 25 years to repay the debt. Moreover, during the term of the loan, the amount of fuel tax revenue available would be reduced by $56 million annually, having a direct and long-term impact on future transportation growth and rehabilitation requirements.

Currently interest costs are not eligible under fuel tax grant rules. Should City Council choose this option, the City could pursue an amendment to the fuel tax rules to allow interest, or alternatively another funding source would be required for the interest.

Scenario 2: Growth Reallocation/Tax Levy Increase Scenario (recommended)

This scenario calls for a tax levy increase of 0.5 per cent annually for seven years (2012-2018) to ease the burden of having to service $806 million ($56 million per year for 25 years) of debt solely with fuel tax dollars. Repaying the debt with a combination of tax levy and fuel tax, frees up fuel tax dollars that would have otherwise been unavailable over the term of the loan for transportation growth and rehabilitation requirements.

Another advantage of using tax levy to service a portion of the debt is that once the debt is paid, the $37 million in the tax base could be used for the LRT life cycle costs.

Scenario 3: Growth / Rehabilitation Reallocation; No Tax Levy Increase Scenario (not recommended)

This scenario requires reallocating $200 million from growth projects and $200 million from rehabilitation projects to LRT.

While reallocating money from growth means deferring new projects, taking money from rehabilitation has more significant long term consequences.

From a financial perspective postponing rehabilitation prevents maintaining current levels of investment which creates backlogs and leads to higher replacement costs. From a condition and risk perspective, postponing rehabilitation results in assets deteriorating further during the deferral period, thereby increasing the City’s liability.

As noted, rehabilitation is already 59 per cent underfunded, and while progress is being made in reducing the infrastructure backlog, our investment in rehabilitation is still falling short by about $168 million per year.