

# Staff Report for Decision

DATE OF MEETING March 18, 2019

AUTHORED BY LAURA MERCER, ACTING DIRECTOR, FINANCIAL SERVICES

SUBJECT 2018 SURPLUS ALLOCATION

## **OVERVIEW**

### **Purpose of Report**

To provide Council information regarding the allocation of the 2018 operating surplus.

### **Recommendation**

That Council approve the allocation of the 2018 operating surplus as follows:

1.	General Fund	
	a. Property Purchase Reserve	\$ 1,400,000
	b. General Capital Reserve	1,600,000
	c. General Financial Stability Reserve	1,292,000
	d. Unallocated General Surplus	276,700
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		\$ 4,568,700
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2.	Sewer Fund	
	a. Sewer Reserve	\$ 675,000
	b. Unallocated Sewer Surplus	64,000
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		\$ 739,000
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3.	Water Fund	
	a. Water Distribution Reserve	2,000,000
	b. Unallocated Water Surplus	287,900
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		\$ 2,287,900
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## **BACKGROUND**

The compilation of the 2018 draft financial statements is in progress and the audit by KPMG LLP will start on 2019-MAR-25. In preparing the financial statements, staff needs to allocate the surplus prior to finalization of the audit.

Any remaining operating surplus funds are considered unallocated surplus and can be used to fund unexpected future liabilities.

The City of Nanaimo accounts for its budgets within three funds: general fund, sewer fund and water fund.

The unaudited financial results for the year ended 2018-DEC-31 are as follows for each of the funds:

### **General Fund**

In the general fund the surplus was \$4,568,654 at 2018-DEC-31. This represents 3% of the budget.

The surplus is made up of the following major variances:

Type	Amount	Explanation
Wages and Benefits	\$1,245,800	Vacant positions throughout the City
Revenues:		
• Business Licenses	134,400	Higher than anticipated revenues
• Building Permits	728,200	Higher than anticipated revenues
• Interest Income	728,600	Higher interest income due to rising interest rates
• Grants In Lieu	179,100	Higher than anticipated revenues
Contracted Services	449,200	Unspent budget
General Contingency	261,200	Unspent contingency
Vancouver Island Conference Centre	187,300	Higher than anticipated revenues
Operating Projects	180,200	Variance from operating projects that came under budget or were cancelled
Hardware & Software licenses & Maintenance	179,900	Expenditures were less than anticipated
Legal Costs	(581,300)	Higher than anticipated legal costs; \$203,500 is offset by the vacant Solicitor position
Utilities	(290,300)	Higher than anticipated Hydro and water/sewer costs partially offset by lower heating costs
Security	(146,500)	Higher security costs mainly due to additional night patrols at the conference centre and additional patrols in City parks

Staff propose the 2018 general fund surplus be allocated to reserves as follows:

### **Property Acquisition Reserve**

**\$1,600,000**

The property purchase reserve has allowed Council in the past to make strategic land purchases including the Linley Valley property, the Port Drive waterfront site, and the School District land purchases. This reserve allocation will allow flexibility for any future land purchase that Council wishes to make, which may include land for affordable housing projects.

### **General Capital Reserve**

**\$ 1,400,000**

This will increase the General Capital Reserve and provide Council with the maximum flexibility in the future. These funds could be used, in whole or part, for any future capital project that is a Council priority.

### **General Financial Stability Reserve**

**\$ 1,292,000**

### **Temp GIS Position - \$92,000**

In the 2019-2023 Financial Plan that was adopted on 2019-JAN-14, a temporary GIS position was approved. Council instructed this position to be funded from prior year surplus. The estimated cost of this temporary position is \$92,000.

### **Waterfront Walkway Feasibility Study – \$400,000**

Currently the waterfront walkway project is in the budget and is planned to be funded from borrowing over the next several years. Staff would like to explore the Northfield walkway alternatives presented in the value engineering study and investigate the feasibility of options presented. This cost of this work will be around \$400,000.

### **Gallows Point Dock & Ramp Repairs - \$100,000**

As a result of the severe windstorms experienced in late December 2018 along with previously identified repairs, a project for Gallows Point pier on Protection Island needs to be added to the 2019-2023 Financial Plan. The Gallows Point boat ramp is a critical infrastructure component that provides the only vehicle access to Protection Island and as such we need to undertake immediate repairs. The cost of this work is estimated to be \$100,000.

### **Post Employment Benefits - \$700,000**

Per Public Sector Accounting Board (PSAB) requirements, the City must to account for the cost of post employment benefits in the financial statements. The City hires an actuarial consulting firm to value the present day cost of these benefits and we adjust the liability each year to their estimate. In previous years we have not budgeted for this or put money aside in a reserve to fund future year costs. Our current practice has been to use current year surplus to cover any change in the liability. By putting money aside in a reserve each year this reduces the reliance on current year surpluses. The three (3) year average of liability adjustments is approximately \$700,000.

### **Unallocated Surplus**

**\$ 276,700**

The remaining balance will be used to increase the unallocated surplus balance. The current balance of the general unallocated surplus account is \$5,499,908.

### **Sewer Fund**

The sewer fund recorded a surplus of \$739,000 at 2018-DEC-31. This represents 16% of the budget.

User fees relating to sewer use were higher than anticipated by \$ 368,000. An unspent sewer contingency of \$60,000 and \$343,000 from debt costs made up the majority of the remaining variance. The debt variance is due to a timing difference between when the budget anticipated borrowing and when we actually borrowed. The combination has enabled \$675,000 to be transferred to the sewer reserves for future projects. The remaining increase will be allocated to the unallocated surplus.

The current balance of the sewer unallocated surplus account is \$6,834,001.

### **Water Fund**

The water fund recorded a surplus of \$2,282,600 at 2018-DEC-31. This represents 20% of the budget.

User fees relating to water use were higher than anticipated by \$649,000. An unspent water contingency of \$100,000, \$1,330,300 in unplanned water connection revenue from Lantzville and \$218,600 from position vacancies made up the majority of the remaining variance. The combination has enabled \$2,000,000 to be transferred to the water reserves for future projects. The remaining increase will be allocated to the unallocated surplus.

The current balance of the water accumulated surplus account is \$5,545,157.

### **Summary**

If a municipality has a small surplus it means that tax rates were appropriately set to meet current year operations. However, it does not provide any excess monies to be transferred to reserves for the funding of future projects or cover any unexpected operating costs that may occur.

If low surplus values are sustained year after year, tax rates can potentially become more volatile as a larger percentage of funding for unexpected events and/or projects will need to come from current year taxes rather than reserves.

In 2018, the City of Nanaimo's accumulated surplus of all 3 funds was \$7,595,600. By transferring these excess surplus funds to reserves this year it means that the need for future year tax increases are mitigated as these monies can be used to cover any unexpected operating costs, drops in revenue sources or fund future projects.

In order to help stabilize future funding sources and minimize the impact on tax rates, Staff are working to establish a Reserves and Reserve Fund Policy. This policy would provide guidance with respect to the development, maintenance and use of City Reserve Funds. The policy would also institute minimum and maximum values, where appropriate, to ensure levels of reserves are on hand at any given time.

The primary objectives of the reserve policy would be to support financial resiliency by:

- Providing funds for operating emergencies
- Ensuring sustainable funding for infrastructure
- Ensuring stable and predictable property tax levies

## **OPTIONS**

1. That Council approve the allocation of the 2018 operating surplus as follows:

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- **Budget Implication:**

- i. \$6,965,000 was reserved to fund general, sewer and water projects and operations in the future
- ii. \$630,600 of general, sewer and water surplus amounts were used to increase unallocated surplus balances

- **Strategic Priorities Implication:**

Asset Management: Reserving current year surplus will aid in the funding of future major maintenance and planned lifecycle replacement costs.

Taking responsibility: Reporting to the public the status of the current year operating results with the goal of building trust.

2. That Council direct specific surplus funds to other priorities. |

### **SUMMARY POINTS**

- The general fund recorded an operating surplus of \$4,568,700 or 3% of approved budget in 2018.
- The Sewer Fund recorded an operating surplus of \$739,000 or 16% of approved budget in 2018.
- The Water Fund recorded an operating surplus of \$2,287,900 or 20% of approved budget in 2018.
- Staff is working on establishing a Reserve and Reserve Fund Policy in 2019 to provide guidance with respect to the development, maintenance and use of City Reserve Funds to ensure appropriate funding levels are available at all.

**Submitted by:**

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