

# Staff Report for Decision

DATE OF MEETING | April 11, 2018 |

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**SUBJECT | 2017 SURPLUS ALLOCATION**

## **OVERVIEW**

### **Purpose of Report**

To provide the Finance and Audit Committee information regarding the allocation of the 2017 operating surplus. |

### **Recommendation**

That the Finance and Audit Committee recommend that Council approve the allocation of the 2017 operating surplus as follows:

1.	General Fund	
	a. Property Purchase Reserve	\$ 1,100,000
	b. General Capital Reserve	752,919
	c. General Financial Stability Reserve	500,000
	d. RCMP Contract Adjustment Reserve	247,081
	e. Unallocated Water Surplus	112,000
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		\$ 2,712,000
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2.	Sewer Fund	
	a. Sewer Reserve	\$ 400,000
	b. Unallocated Sewer Surplus	69,000
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		\$ 469,000
		=====
3.	Water Fund	
	a. Water Supply Reserve	\$ 180,000
	b. Water Distribution Reserve	720,000
	c. Unallocated Water Surplus	112,000
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		\$ 1,012,000
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## **BACKGROUND**

The compilation of the 2017 draft financial statements is in progress and the audit by KPMG LLP started on 2018-MAR-26. 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 2017-DEC-31 are as follows for each of the funds:

### **General Fund**

In the general fund the surplus was \$2,712,000 at 2017-DEC-31. This represents 2% of the budget.

Staff propose the 2017 general fund surplus be allocated to reserves as follows:

<b>Property Acquisition Reserve</b>	<b>\$1,100,000</b>
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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.

<b>General Capital Reserve</b>	<b>\$ 752,919</b>
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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.

<b>General Financial Stability Reserve</b>	<b>\$ 500,000</b>
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In 2017 the Provincial Government announced that it was phasing out the MSP program and then in 2018 announced they were replacing it with an Employer Health Tax. This new employer health tax would become effective for the 2019 fiscal year. The MSP premiums will be completely phased out in 2020. This results in an estimated additional \$1.1 million of costs in 2019 to cover both the MSP premiums and the new employer health tax. This surplus allocation will help smooth the tax impact of the transition from MSP premiums to the new employer health tax in 2019.

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**RCMP Contract Adjustment Reserve**

**\$ 247,081**

At the 04-Apr-2018 Finance and Audit Committee Meeting, the Committee directed staff to reduce the budget estimate for the RCMP contract from 93% to 92%. This reduction of \$247,081 was to be taken out of the 2017 surplus and allocated to the RCMP Contract Adjustment Reserve. This surplus will be a funding source for any contract variance.

**Unallocated Surplus**

**\$ 112,000**

The remaining balance will be used to increase the unallocated surplus balance. The current balance of the general unallocated surplus account is \$5,499,909.

**Sewer Fund**

The sewer fund recorded a surplus of \$469,000 at 2017-DEC-31. This represents 10% of the budget.

User fees relating to sewer use were higher than anticipated by \$318,000. An unspent sewer contingency of \$60,000 made up the majority of the remaining variance. The combination has allowed up to \$400,000 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 \$1,012,000 at 2017-DEC-31. This represents 8% of the budget.

User fees relating to water use were higher than anticipated by \$884,000. An unspent water contingency of \$100,000 made up the majority of the remaining variance. The combination has allowed up to \$900,000 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**

While having a small surplus means that tax rates were appropriately set to meet current year operations, 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.

By transferring excess surplus funds to reserves each 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.

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 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 the Finance and Audit Committee recommend that Council approve the report allocation of surplus as presented.
  - **Budget Implication:**
    - i. \$3,900,000 was reserved to fund general, sewer and water projects and operations in the future
    - ii. \$293,000 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 the Finance and Audit Committee recommend that Council direct specific surplus funds to other priorities.

## **SUMMARY POINTS**

- The general fund recorded an operating surplus of \$2,712,000 or 2% of approved budget in 2017.
- The Sewer Fund recorded an operating surplus of \$469,000 or 10% of approved budget in 2017.
- The Water Fund recorded an operating surplus of \$1,012,000 or 8% of approved budget in 2017.
- Staff is working on establishing a Reserve and Reserve Fund Policy in 2018 to provide guidance with respect to the development, maintenance and use of City Reserve Funds to ensure appropriate funding levels are available at all times

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**Submitted by:**

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