Municipal LGDE Help Manual

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BRITISH COLUMBIA
Ministry of Community, Sport and Cultural Development

Table of Contents

6. Debt Schedules

This part of LGDE tracks the total debt level of a local government that arises from borrowing in accordance with section 175 (liabilities under agreement), interim financing through section 181, adopted bylaws in accordance with sections 178 (short-term capital borrowing) and 179 (loan authorization bylaw) of the *Community Charter* or S.236 (borrowing bylaw) of the *Vancouver Charter*. This part of LGDE also tracks any other long-term commitments that may not be included in the Statement of Financial Position. All of this information is used to calculate the borrowing power of the municipality.

In calculating liability servicing capacity, we add all estimated servicing costs of off balance sheet items that may impact a municipality's solvency. These off balance sheet items are normally included in the notes to the financial statements and fall into three broad categories: Authorized but Unissued Borrowing, Guarantees, and Long-Term Agreements.

6 (a) Analysis of Authorized Debt and Short Term Capital Borrowing (Schedule B1)

This schedule provides a check of the amount of debt reported in long-term liabilities on the Statement of Financial Position as well as providing detail regarding the amount of short term capital borrowing and the total amount of authorized but unissued borrowing. The second part of the schedule reconciles the total debt at the beginning of the fiscal period to that at the end with changes to debt resulting from new borrowing and debt repayment. With the exception of Authorized but Unissued Debt (which is not shown on any of the other Schedules) the information in Schedule B1 should reflect the information previously entered in the Statement of Financial Position - Schedule A2.

Unmatured Long-Term Debt Issued by the Local Government (Line a)
For the City of Vancouver, this line should include all unmatured debt issued under the authority of the *Vancouver Charter* (except any issuing under S.239A, which should be included in Line b of this schedule).

For all other local governments, this line item should equal the unmatured portion of debt issued under the authority of a loan authorization bylaw (S. 179) but **not** issued through the MFA (S.182) or temporary financing (S.181). This would generally include borrowing under the authority of a loan authorization bylaw (S.181) and through a government loan program (e.g. CMHC loans and Downtown Revitalization loans).

Also, if a local government has inherited an improvement district debt, the remaining balance of this debt may be included in this line.

Unmatured Long-Term Debt Issued by the MFA (Line b)
This line item should equal the unmatured portion of debt issued either directly or indirectly through the MFA. This line should include all unmatured debt issued under section 182 (security issuing bylaws) of the *Community Charter* or section 239A (borrowing through the GVRD) of the *Vancouver Charter*. This also includes any interim capital financing through the MFA (S.181).

Authorized but Unissued Long-Term Debt (Line c)
Authorized but unissued borrowing occurs where a municipality has the authority to borrow under bylaw (section 179 of the *Community Charter* or section 236 of the *Vancouver Charter*), but has not yet issued securities under section 182 of the *Community Charter* or section 239 and 239A of the *Vancouver Charter* **or** received a loan under a government loan program. This amount represents legally authorized, but unutilized, borrowing authority of the local government that is not recognized in the Statement of Financial Position and therefore must be recorded here to be included in the Liability Servicing Limit calculations.

It also should include any remaining debt of another party that has been guaranteed under *Community Charter* S. 175.

Capital Lease Liabilities (Line d)
This amount should equal the total capital leases summarized in Line p of schedule A2 (Statement of Financial Position). For more information about capital leases and their treatment, see section 5(a)(ii) - Liabilities (Schedule A2).

Short Term Capital Borrowing Amount Issued (Line e)
Include in this line the total amount borrowed under section 178 of the *Community Charter* less the balance paid to date. Do not include any amounts authorized under section 178 that are not actually borrowed (this is addressed in Line f).

Authorized but Unissued Short Term Capital Borrowing (Line f)
This line represents the total amount the local government has the authority to borrow under section 178 of the *Community Charter* but has not yet borrowed. As the debt has not yet been incurred, it is not captured in the Statement of Financial Position and must be recorded here for inclusion in the Liability Servicing Limit calculations.

Total Debt Issued (Line g)
Totals long-term debt issued by the local government and MFA as well as borrowed through short-term capital borrowing. This is a formula cell and equals the total from lines a b, d, e of Schedule B1.

Total Debt Authorized but Unissued (Line h)
This line item is the total debt authorized by loan authorization bylaws but not issued by security issuing bylaws. This line item is also the total amount authorized by short term capital borrowing bylaws but not yet borrowed. This is a formula cell that totals lines c and f.

Total Debt (Line i)
This is the total of all authorized debt both long-term and short-term whether issued or not.

Reconciliation
This section of the schedule reconciles the total debt at the beginning of the fiscal period to that at the end with changes to debt resulting from new borrowing and debt repayment. Information on all the types of debt that were included in Lines a, b, c, and e should be entered into the reconciliation section.

Long Term Debt at Beginning of Year (Line j)
This is the total of all authorized debt at the beginning of the year. It should equal the value calculated for Line g in the previous year's LGDE.

Proceeds from Issue of Debt (Line k)
Local governments are not allowed to run sustained deficits in accordance with section 165 of the *Community Charter*. Therefore any long-term debt of a local government is to support capital asset financing.

This line item represents the portion of purchases of tangible capital assets. (Form A5 line b), for the current reporting period, that were financed through new debt.

This line item represents the value of financial proceeds from borrowing received by the municipality from the MFA (or other financing organizations) during the accounting period. In accordance with PS 1200.090 the LGDE forms differentiate the reporting methods for revenue and the financial proceeds from borrowing (including debenture issues). Borrowing proceeds do not flow through the Statement of Operations (Schedule A3).

Debt Repayment (Line L)
A principal payment is a repayment of the principal component of municipal debt (this can include the principal portion of MFA debenture debt, bank loans, serial debt (e.g. mortgages), capital leases, short term capital borrowing, interim financing and other capital financing arrangements under agreement). **This line item does <u>not</u> include interest payments or MFA actuarial adjustments.**

In accordance with PS 1200.089, debt repayment is not considered an "Expense" and therefore does not flow through the Statement of Operations (Schedule A3).

Actuarial Adjustments (Line m)
This line item represents the annual actuarial adjustments on MFA debenture debt. The actuarial adjustments reflect annual investment gains from the sinking funds (and other debt retirement funds) held by the MFA. Because these sinking funds are held by an external body (i.e. the MFA), they are not reported in the local government's Statement of Financial Position. Instead the actuarial adjustment is applied directly against the outstanding debenture debt of the local government.

Long Term Debt at End of Year (Line n)
This line is auto-calculated as the sum of lines j and k less the sum of lines L and m. The amount must equal line g above.

6 (b) Other Commitments Not Included in the Statement of Financial Position (Schedule B2)

This is a roll up schedule that includes any material commitments of the local government that are **not** included in the Statement of Financial Position. These off balance sheet items are represented by Loan Guarantees (Schedule B2a and Line a), Agreements not on Other Schedules (Schedule B2c and Line b) and Long-Term Agreements (Schedules B2d, B2e, B2f and Lines c, d and e).

The amounts in this schedule are used in calculating the liability servicing capacity.

Guarantees Under Agreement (Schedule B2a and Line a)
Guarantees are the result of contractual obligations freely entered into by the municipality. Under the *Community Charter*, loan guarantees may be established by bylaw (S.179) or by agreement (S.175). In either case, the guarantee must be recorded in the liability servicing formula.

The amount to be recognized as a guarantee is the lesser of the
- initial guarantee under bylaw or agreement, or;
- the amount of remaining third party debt under guarantee.

Loan Guarantees Under Bylaw (Community Charter S.179) (Schedule B2a)
The liabilities in this schedule are already recorded as Authorized but Unissued Debt on Schedule B1, line g, and used to reduce the liability servicing capacity. However, we only want to capture the amount of outstanding third party debt remaining under guarantee. In order to do this, we must reduce the total guarantee by the amount of third party debt that has already been retired, this equals the following:

= Amount of loan guarantee bylaw - remaining third party borrowing

Loan Guarantees under Agreement (CC S.175) (Line a) (Schedule B2b)
This line item is a formula cell that links to the total from Schedule B2b (Loan Guarantees under Agreement). These guarantees do not require a bylaw, thus, are not captured under "Authorized but Unissued Borrowing". As such, we will only include the remaining third party liability guaranteed by the agreement. The annual debt servicing cost in relation to loan guarantees is determined by dividing the remainder of the debt under guarantee by the remaining agreement term in years.

Agreements not on Other Schedules (Line b) (Schedule B2c)
This line item is a formula cell that links to the total from Schedule B2c (Agreements not on Other Schedules). It includes the estimated annual cost of servicing capital or contingent portions of any off balance sheet commitments of the local government. An example of this would be the yearly expenditure associated with a P3 (public-private

partnership) agreements. The annual debt servicing cost in relation to the agreements not on other schedules is determined by adding the remaining principal and a residual value and dividing this total by the remaining term in years.

There are 20 rows in Schedule B2c, enter one agreement per row. If your local government has more than 20 agreements, enter the 19 most material agreements in the first 19 rows and sum all remaining agreements in row 20.

Further explanation of long term agreements can be found in the next section.

Long Term Agreements (Lines c, d, and e) (Schedules B2e, d, and f)

These are formula cells that link to the totals from Schedules B2d, B2e, and B2f (Long Term Liabilities Under Agreement). These are long term facility agreements that are not capitalized on the financial statements. All such long term agreements must be included in the liability servicing liming, with the following exceptions:

Exceptions: There are several types of agreements that will not be included in the liability servicing formula, including:

i) immaterial agreements,
ii) union collective agreements,
iii) individual employment contracts,
iv) agreements that the municipality may cancel on favourable terms,
v) operating agreements

i) **Immaterial Agreements**

Some agreements are for immaterial amounts. To prevent having to track and include immaterial agreements in the liability servicing formula, a materiality limit is set. Any agreement with an annual payment below the materiality limit does not need to be recorded in the liability servicing limit. **The materiality limit is equal to $30,000;** however, the limit may be decreased if $30,000 is a material amount to the local government in question. Professional judgment should be used to determine individual materiality amounts.

ii) **Collective Agreements**

Union agreements deal with the cost of staffing municipal services. Such staffing costs are both variable and part of day-to-day operations. Thus, these costs should not be included in the liability servicing limit.

iii) **Individual Employment Contracts**

These are employment contracts separate from the collective agreement. These contracts are not included in the liability servicing limit for the same reasons as the omission of union contracts.

iv) **Agreements that the Municipality may Cancel on Favourable Terms**

Some long-term agreements may allow the municipality to cancel the agreement on favourable terms. Agreements that meet the following criteria do not need to be included in the liability servicing limit calculation:

- the municipality may cancel the agreement on no more than one year's advance notice
- there is no penalty or assumption of liability in excess of the annual cost of the agreement for the municipality.

v) **Operating Agreements**

These are agreements with respect to the day-to-day operations of the local government that may be contracted to an outside party rather than be performed by the local government. These costs are not included in the liability servicing limit so that a local government who provides the service themselves does not receive a bonus over one who contracts the service out.

Completing Schedules B2d, e and f (Calculating the Amount of the Long-Term Agreement)

Please follow the instructions on these schedules. There is one schedule per agreement. If your municipality has more than three agreements, enter the three most material agreements in these schedules. All remaining agreements should be added to Schedule B2c.

For each agreement schedule, the total liabilities under agreement are calculated by discounting the annual expenditures over the remaining term of the agreement. The discount rate used will be 5% (based on the MFA sinking fund rate).

Example calculation:

Annual Expenditure	= E	=$100,000
Remaining Term	= N	= 5 years
Discount Rate	= D	= 5%
Present Value	= PV	

$$PV = \frac{E(E_N)}{(1+D)^N} \qquad = \underline{\$432,950}$$

Variable Versus Fixed Payments: Some agreements have a preset fixed annual payment and may be calculated using the above formula. However, if the annual agreement payments are not fixed (for example, an annual revenue guarantee agreement) an estimate must be used for the annual expenditure under agreement. This is done by **averaging the previous three years' expenditures**. If three years of data is unavailable (i.e. a brand new agreement) the following is done:

- Year one of the agreement - use the budgeted (annualized) expenditure figure for the first year, or other reasonable estimate;
- Year two of the agreement - use the actual (annualized) expenditure figure from year one;
- Year three of an agreement - use the average of the actual (annualized) expenditure figures from years one and two.

The average expenditure is then discounted over the remaining term of the agreement.

Total Debt Servicing Cost from Other Liabilities (Line f)

This is a formula cell that totals the debt servicing cost of off balance sheet liabilities. It is the sum of lines a, b, c, d and e.

Actual Debt Servicing Cost (Line g)

This is a formula cell that sums all of the recorded interest expenditures from the Statement of Financial Operations and the debt principal payments for the year. It does not include actuarial adjustments because these are not expenditures of the local government; they simply represent a reduction in the amount of principal owed. The formula is schedule A3 lines k2+l2+m2+n2+o2+p2+q2+r2+s2+t2+Schedule B1 Line L.

Estimated Debt Servicing Cost on Unissued Debt (Line h)

This cell estimates the annual servicing cost of authorized but unissued debt. It is a formula cell which takes the total amount of authorized but unissued debt from schedule B1 Line g, subtracts the total amount of any loan guarantees under bylaw that are no longer under guarantee from Schedule B2a Total, and multiplies the remaining amount by 0.09 to determine an estimate of the annual servicing cost. We have chosen a factor of 0.09 for the estimation of annual servicing cost as this is symbolic of 20 year 6% debt. Twenty years is the average term of local government borrowing and 6% is a conservative estimate based on current Municipal Finance Authority financing rates.

Total Debt Servicing Cost (Line i)

This is a formula cell which calculates the total debt servicing cost for the year from all sources. It adds the estimated servicing cost for off balance sheet liabilities (Line f), the actual debt servicing cost paid or payable during the year (Line g) and the estimated amounts for authorized but unissued debt (Line h).

6 (c) Annual Liability Servicing Limit (Schedule B3)

The *Municipal Liabilities Regulation* (B.C. Reg. 254/2004) was passed by Cabinet and became effective on June 10, 2004. The regulation establishes limits on local governments' annual liability servicing cost and establishes a method for determining both the limit and the annual cost. This schedule is made up mainly of carry-forward items from other schedules which are used to calculate the annual liability servicing limit for the following year.

The liability servicing limit is calculated as 25% of a municipality's controllable, sustainable revenues. Some specific examples include: sale of services, provincial unconditional grants, casino revenues, investment income and own purposes tax revenues with a cap on class four properties. These revenues are either directly controllable by the local government or there is very little doubt that they will continue into the future. Specifically excluded from the allowable revenues are conditional grants, DCCs, actuarial adjustments from the MFA and Hotel tax. These items are excluded because their value can vary significantly from year to year and because they are generally related to fixed expenditures, so they are unavailable for other purposes such as servicing debt.

Own purpose tax revenues are controllable by the local government and sustainable, so they are included in the calculation, however, class 4 property taxation is capped to prevent an over-reliance on major industry to meet the operating needs of the municipality. In this way, the municipality will be protected from possible debt default if the class 4 property is no longer able to meet its tax obligations.

The cap is two-fold; it is a cap on the assessed value and a cap on the tax rate. The cap on assessed value states that the assessment may not exceed 20% of the total municipal assessment. The lesser of the actual class 4 assessment or 20% of the total municipal assessment becomes the assessed value used to calculate the tax revenue. The cap on the rate limits the tax rate to the lesser of the actual rate or the provincial average. The provincial average is determined by taking the total class 4 general municipal revenues for the entire province and dividing it by the total class 4 general municipal assessment for the entire province. This gives a rate that would have to be charged to every property in order for the same total amount of revenue to be earned. Local governments involved in tax sharing agreements must use derived assessments and tax rates that include or exclude the amount of tax sharing.

Value for Calculation (Line a)

This represents the lesser of the actual class 4 assessed value (Line a1) for the year and 20% of the total assessed value (Line a3) for the year and is the amount that will be used to calculate the allowable class 4 revenues.

Value for Calculation (Line b)

This represents the lesser of the actual class 4 general municipal tax rate (Line b1) and the provincial average tax rate (Line b2) as described above. It is the tax rate that will be used to calculate the allowable class 4 revenues for the year.

Municipal Revenues (Line c)

This is a formula cell that collects controllable, sustainable revenue information from Schedule A3 (Statement of Financial Operations) and Schedule A4 (Statement of Property Taxation). It equals:

> Sale of Services (Line b) + Federal Govt/Agencies Unconditional Transfers + Provincial Govt/Agencies Unconditional Transfers (Line c4) + Other Provincial Government Transfers (Line c5) + Regional and Other External Unconditional Transfers (Line c7) + Investment Income (Line d) + Other Revenue (Line i) (All lines on Schedule A3 Statement of Financial Operations) + Total Own Purpose Taxation (Line f) – Hotel Tax (Line d2) (All lines on Schedule A4, Statement of Property Taxation) – Actuarial Adjustment (Line m – Schedule B1).

Less: Actual Class 4 Revenue (Line d)

This amount is determined by dividing the class 4 assessed value (line a1) by 1,000 and multiplying by the class 4 tax rate (line b1). It is subtracted from the municipal revenues because the total amount of all taxation revenues are included in the municipal revenue, but the full amount of class 4 revenues may not be included in the revenues due to the cap.

Plus: Capped Class 4 Revenue (Line e)

This amount is determined by dividing the assessed value for calculation (line a) by 1,000 and multiplying by the class 4 tax rate value for calculation (line b). It is added to the municipal revenues so that the capped class 4 taxation revenues are included.

Less: Amounts Transferred to Others (Line f)

This is the only line on this page that allows numbers to be entered. It is primarily for use by municipalities who transfer tax sharing revenues to other municipalities and have not included the amount of the transfer on Schedule A4. However, it can also be used to reflect any other necessary adjustments that have not been otherwise accounted for. **Caveat:** The Ministry reserves the right to request clarification of any amounts entered on this line.

Total Revenues (Line g)

This expresses the controllable, sustainable revenues of the local government to be used in the calculation of the liability servicing limit. It is calculated as Line c – line d + line e – line f.

Liability Servicing Limit (Line h)

This is the total amount a local government can spend to service its capital obligations and guarantees for the year. It is calculated as 25% x Total Revenues from Line g.

Actual Debt Servicing Cost (Line i)

This is a carry forward cell. It equals Line g on Schedule B2.

Estimated Cost from Off-Balance Sheet Liabilities (Line J)

This is a carry forward cell. It equals Line f on Schedule B2.

Estimated Cost on Unissued Debt (Line k)

This is a carry forward cell. It equals Line h on Schedule B2.

Total Liability Servicing Cost (Line l)

This is the total amount of actual and estimated annual liability servicing cost for the local government for the year. It is the sum of the actual debt servicing cost (Line i), estimated cost from off-balance sheet liabilities (Line J) and estimated cost on unissued debt (Line k).

Liability Servicing Capacity Available (Line m)

This is the unused liability servicing limit as at December 31. It is determined by subtracting the total liability servicing cost (Line l) from the liability servicing limit (Line h). To obtain an estimate of the amount of debt represented by this figure, the number can be divided by 0.09. This gives the amount of debt which could be borrowed for twenty years at 6% interest that is equivalent to the available capacity.

In addition to establishing the liability servicing limit, the *Municipal Liabilities Regulation* (B.C. Reg. 254/2004) also exempts some liabilities from the requirement to seek elector approval, including the establishment of an approval free liability zone. The approval free liability zone is an attempt to balance the objective of municipal accountability against the need for municipalities to conduct efficient operations. It is calculated as 5% of the controllable, sustainable revenues from line g above. This is the same as 20% of the liability servicing limit from line h above. The approval free liability zone is limited to the first 5% of revenues only. If the existing liability servicing cost already exceeds this amount, there is no approval free room and elector approval must be obtained for all new obligations. If the servicing cost of the proposed liability is greater than the remaining approval free capacity, elector approval must be obtained. Only if the entire servicing cost of the proposed obligation combined with the existing servicing cost is within the 5% of revenue threshold, can the obligation be undertaken without obtaining elector approval. Also, use of the approval free zone is optional, not mandatory. Local governments may seek elector approval even if not required to do so.