

**REPORT TO THE REGIONAL PARKS COMMITTEE
MEETING OF WEDNESDAY, SEPTEMBER 22, 2021**

SUBJECT Regional Parks Land Acquisition and Infrastructure Financing Strategy

ISSUE SUMMARY

To develop land acquisition and infrastructure financing strategies key to the ability to execute investments and manage a sustainable service.

BACKGROUND

At the June 23, 2021, Regional Parks Committee meeting, staff were directed to report on a recommended financing option for future investments in land and major capital works that incorporates current financial guidelines.

Operating a long-term sustainable service relies on balancing priorities in operational delivery and the related financial implications. A financing strategy aimed at managing revenue and cash flow can increase capacity and unlock value to enhance the ability to operate and meet service needs.

Through the Finance Committee and the Capital Regional District Board, staff have reported on various decision models and guidelines to inform and influence financial strategies.

1. January 2019: the corporate asset management program and strategy was approved. The approach drives purposeful intervention to manage and maintain asset health through the lifecycle, ensuring long-term service delivery.
2. October 2019: debt term guidelines set optimal financing amortization periods on the basis of value. This report demonstrates a 15 year term as the optimal point of intersection between annual debt servicing costs and total interest expense.
3. July 2021: capital reserve guidelines established optimal savings versus debt financing by correlating the useful life of assets.

The culmination of these reports and other analyses influence both service and budget processes annually.

In relation to regional parks infrastructure, there is an opportunity to optimize both land acquisition and capital investment through a formal financing strategy which uses both savings and debt to invest in value-added service delivery. The strategy enables use of debt in a time where service demand is increasing and interest rates are at historic lows.

The current macro-economic environment supports a leveraged approach to land acquisition and infrastructure. Central banks across the globe rapidly expanded national balance sheets in an effort to combat the economic slowdown induced by the onset of the global pandemic. The Bank of Canada cut the overnight benchmark rate three times since March 2020 and simultaneously deployed a variety of monetary policy tools to expand the money supply. While signs of recovery have reduced the Bank of Canada's measures in recent months, ongoing low interest rates are anticipated.

Due to an indebted Canadian consumer, the Bank of Canada is expected to proceed cautiously in withdrawing monetary stimulus and will likely not allow borrowing rates to rise dramatically. Global capital markets maturity and related arbitrage activity provide nearly instant liquidity sufficient to meeting any return of consumer and industrial demand for goods and services. These factors create a natural cap to how high interest rates may rise in the near future, which provides an important foundational support for a revised land acquisition and infrastructure financing strategy.

This report focuses on outlining a proposed strategy which balances the current and future need for land acquisitions, maintaining capital reserve health, the relationship between leverage and debt affordability, and the integral impact on service delivery.

ALTERNATIVES

Alternative 1

The Regional Parks Committee recommends the Committee of the Whole recommend to the Capital Regional District Board:

That the annual land acquisition levy be used to implement a debt financing strategy for future land acquisitions.

Alternative 2

That this report be referred back to staff for additional information.

IMPLICATIONS

At the November 13, 2019, Board meeting, the land acquisition levy was renewed through 2029. Subsequently, at the meeting of October 28, 2020, the Board resolved to increase the annual land acquisition levy rate per household by \$1 each year through 2025 (from \$20 to \$25).

The 2020-2021 Land Acquisition Strategy states that to be effective, the strategy needs to account for opportunistic acquisition of important lands. The purpose is to:

- meet the need of region's residents now and in the future
- respond to expected population growth
- connect, protect and restore the region's natural resources
- provide areas for residents to connect with nature

The current Land Acquisition Strategy identifies key areas of interest and identifies the overriding concept that bigger natural areas are better and connected natural assets are best.

Developing land acquisition and infrastructure financing strategies is key to staff's ability to execute investments and manage a sustainable service. A successful strategy will enable opportunistic acquisition versus saving for a cash purchase.

Through use of benchmarks established by the capital reserve guidelines, the Regional Parks Service was identified as having a low use of debt to deliver mandated services. Through operational planning, a significant portion of upcoming capital investment was directed for land and infrastructure replacement, which are assets characterized with a long, useful life. Both the

Public Sector Accounting Board (PSAB) and Generally Accepted Accounting Principles (GAAP) do not permit depreciation of land; instead, land holds value in perpetuity.

The aforementioned capital reserve guidelines balance the implications of savings and borrowing, recommending an optimal blend or ratio as part of a financing strategy. When evaluating the reserve balance guidelines, the Regional Parks Service has significant borrowing capacity, and increased use of debt can be a tool to manage annual costs. For any asset, when the rate of appreciation exceeds the cost of borrowing, value growth and interim utility result. The current land acquisition funding strategy is a pay-as-you-go savings model which sees annual revenues set aside until the fund has a sufficient balance for purchases.

Appendix A presents a comparison between lands purchased today versus 15 years in the future. The analysis demonstrates the magnitude of value creation in the spread between land appreciation and cost of borrowing (net of holding costs, interest and inflation).

With the use of borrowing, the annual \$20 per household levy translates to an annual \$4 million revenue stream that can be used to debt service up to \$50 million worth of purchases. In 15 years, using historic land appreciation rates, the value would be approximately \$119 million. When adjusted for holding and interest costs, the net increase in value could be in excess of \$100 million.

Conversely, saving the annual requisition over the next 15 years would yield approximately \$67 million of purchasing power, translating to 57% of the land mass that could have been purchased today. Table 1 summarizes and compares two approaches based on \$50 million of land acquisition today.

Table 1: Illustrative Example of Financing vs Savings for Land Acquisition

	Financing Strategy	Current Funding Model
# Hectares	1,000 Hectares	563 Hectares
Future Value (Year 15)	\$119M	\$67M
Cost per Hectare	\$50,000 / hc (Today)	\$119,000 /hc (Year 15)
Future Value (Net of costs)	\$100M	\$67M
Present Value	\$74M	\$50M

Through an optimal financing strategy, \$24 million in value for the equivalent dollar expenditures could be added to the regional parks network while simultaneously providing asset utility to the region.

Appendix B provides a graphical representation of the value created through financing in maximizing acquisitions to the cap of \$20 per household in year 0. In this scenario, the Regional Parks Service could immediately acquire \$50 million of land and debt service over the next

15 years with no impact to requisition. After 15 years, the service could acquire an additional \$50 million of land and repeat indefinitely.¹

Recognizing various constraints, Appendix C provides a graphical representation of the value created through financing in phased acquisitions to the cap of \$20 per household through the first 5 years. In this scenario, the Regional Parks Service could acquire up to \$50 million of land and debt service over the next 20 years with immediate savings to requisition through year 5. As borrowing would be phased, debt would mature after year 15 where additional borrowing could be leveraged. This laddering strategy is similar to the financial strategies used in the Capital Regional Hospital District for major capital projects, and the Capital Regional District (CRD) investment holdings for GICs (Guaranteed Investment Certificates).²

Other Considerations

As required by the *Local Government Act*, Section 403 (1), and the *Community Charter*, Section 179, a loan authorization bylaw is required for long term borrowing. All loan authorization bylaws require Board approval, and capital expenditures must be included in the five year financial plan. Staff will continue to report on land acquisitions through the Board and supplement with impacts to annual debt servicing costs and the upper limit of the annual land acquisition levy. Additionally, financial health indicators will continue to be used to monitor liquidity, interest coverage, leverage, and capital reserve health of the Regional Parks Service and the CRD.

CONCLUSION

Staff were directed by the Regional Parks Committee to report on a recommended financing option for future investments in land and major capital works that incorporates current financial guidelines. The CRD corporate asset management program and strategy, debt term guidelines, and capital reserve guidelines inform and influence staff recommendations on financial strategies. The proposed financing strategy is designed to make good use of debt and capital reserves in order to provide sustainable service delivery and budgeting.

RECOMMENDATION

The Regional Parks Committee recommends the Committee of the Whole recommend to the Capital Regional District Board:

That the annual land acquisition levy be used to implement a debt financing strategy for future land acquisitions.

Submitted by:	Nelson Chan, MBA, FCPA, FCMA, Chief Financial Officer
Concurrence:	Larisa Hutcheson, P. Eng., General Manager, Parks & Environmental Services
Concurrence:	Robert Lapham, MCIP, RPP, Chief Administrative Officer

ATTACHMENT(S)

Appendix A: Financial Analysis – Land Acquisition Decision Model

Appendix B: Land Acquisition Decision Model – Maximizing Acquisitions

Appendix C: Land Acquisition Decision Model – Phased Acquisitions

¹ To simplify the illustration, all other variables held constant, including but not limited to annual levy per household, etc.

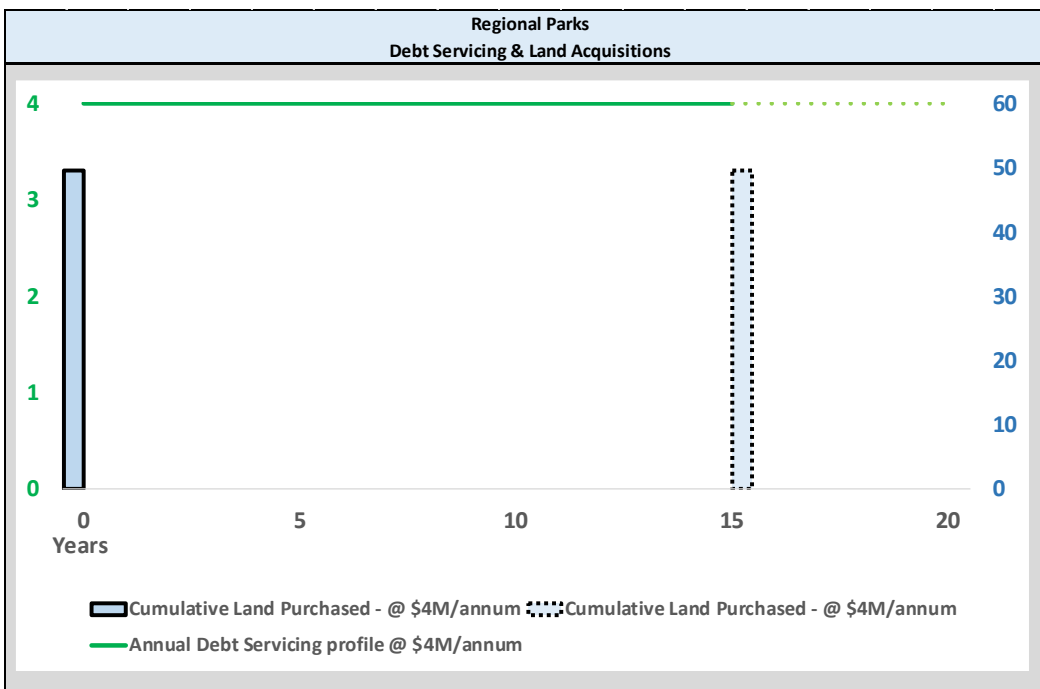
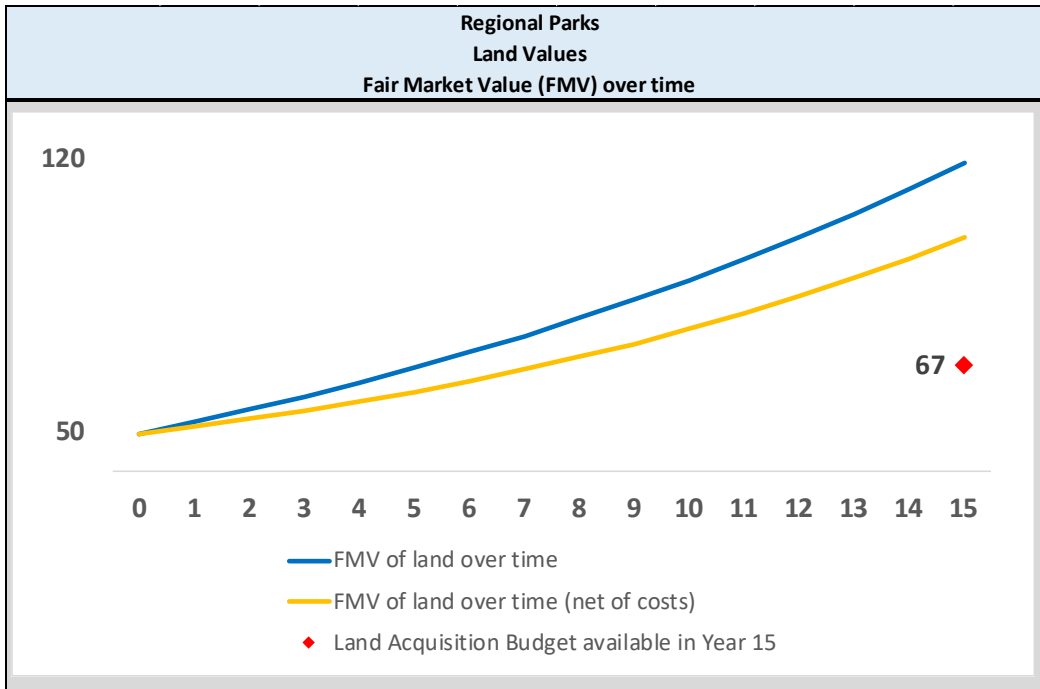
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Appendix A: Financial Analysis – Land Acquisition Decision Model

Assumptions:		Notes
Rate of land appreciation	6.0%	Based on BC Assessment Land data, historic 5 year regional land average appreciation rate
Rate of inflation:	2.0%	Based on BC Stats data, adjusted for forecast
Option 1: Borrow to invest in land today		
Fair Market Value of Land Purchased today:	\$50 million	Land acquisition is based on 100% financing based on maximum principal serviceable by a \$4 million/annum debt servicing budget
<div>Land Values Grow @ 6.0%/year ...</div> <div>↓</div>		
Growth-adjusted land value in Year 15:	\$119 million	Growth of land value over 15 years using rate of land appreciation assumption
<u>Less costs</u>		
Annual Land Holding Costs	\$9 million	Assume 1% of land fair market value acquired today per year and grown at assumed inflation rate. Accounts for cost of security/patrols, insurance etc
Financing Costs (financing rate 2.39%)	\$10 million	MFA 15 year debt @ current indicative rate
Growth-adjusted land value in Year 15 (after costs):	\$100 million	Land value in year 15 less costs
Land value today (after inflation):	<u>\$74 million</u>	
Option 2: Defer land purchase - save reserves over time		
Fair Market Value of Land Purchased today:	\$0	
Annual Reserve Contribution:	\$4 million	Annual reserve contribution assumption
Reserve Balance - Year 15:	\$60 million	\$4 million/annum for 15 years
<u>Plus</u>		
Interest Earned on Reserve Balances	\$7 million	Accounts for investment rate of 1.5% / annum on reserve balance
Land Acquisition Budget available in Year 15	\$67 million	Land acquisition budget available in year 15
Land Acquisition Budget available in Year 15, in today's dollars (after inflation):	<u>\$50 million</u>	
Value added by Option 1 over Option 2:	\$24 million	Difference in option 1 versus option 2 land values in today's dollars

Appendix B: Land Acquisition Decision Model – Maximizing Acquisitions

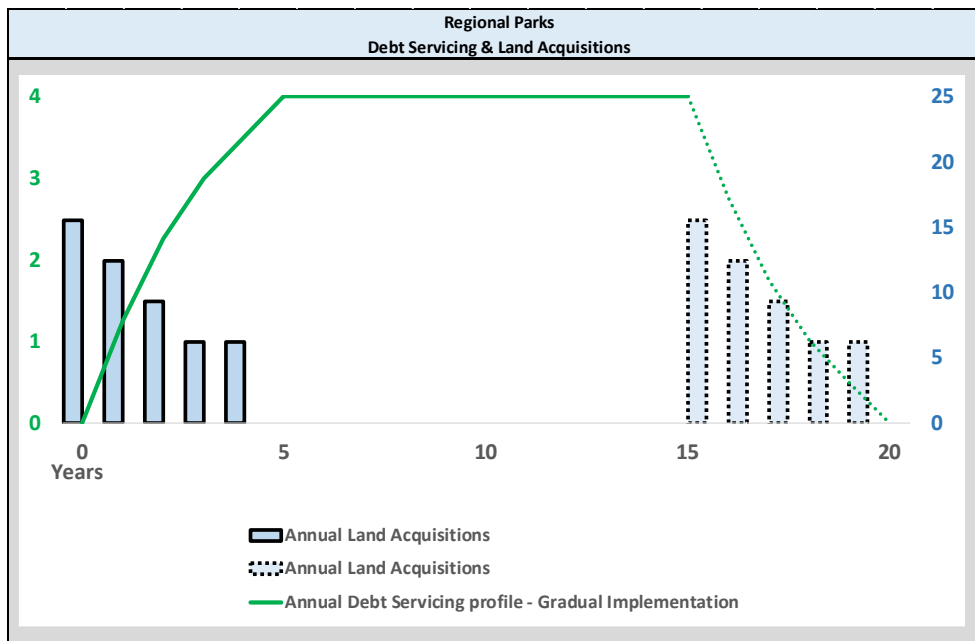
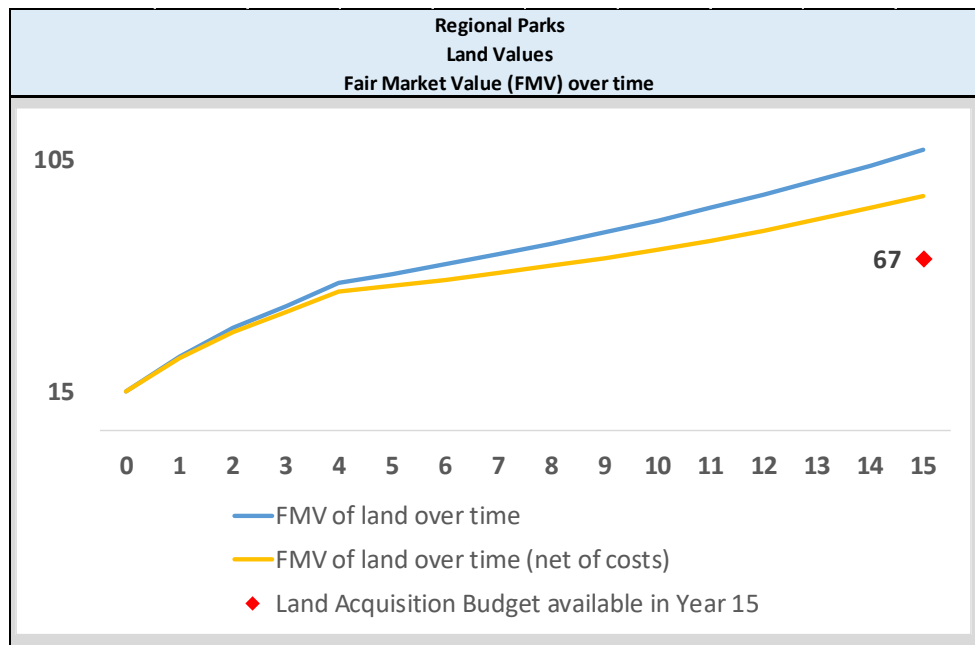
These charts represent the value created through financing in maximizing acquisitions to the annual levy cap of \$20 per household in year 0. In this scenario, the regional parks service could immediately acquire \$50 million of land and debt service over the next 15 years with no impact to requisition. After 15 years, the service could acquire an additional \$50 million of land and repeat indefinitely.¹



¹ To simplify the illustration, all other variables held constant, including but not limited to annual levy per household, etc.

Appendix C: Land Acquisition Decision Model – Phased Acquisitions

These charts represent the value created through financing in phased acquisitions to the annual levy cap of \$20 per household through first 5 years. In this scenario, the regional parks service could acquire up to \$50 million of land and debt service over the next 20 years with immediate savings to requisition through year 5. As borrowing would be phased, debt would mature after year 15 where additional borrowing could be leveraged. This laddering strategy is similar to the financial strategies used in the Capital Regional Hospital District for major capital projects, and the CRD investment holdings for GICs (Guaranteed Investment Certificates).¹



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