



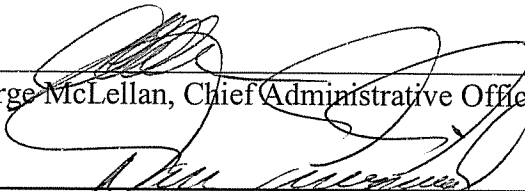
PO Box 1749  
Halifax, Nova Scotia  
B3J 3A5 Canada

9.1.1

**Halifax Regional Council**  
**May 17, 2005**

**TO:** Mayor Kelly and Members of Halifax Regional Council

**SUBMITTED BY:**

  
George McLellan, Chief Administrative Officer

  
Dan English, Deputy Chief Administrative Officer

**DATE:** May 10, 2005

**SUBJECT:** Financial Policy Respecting Interest on Bridge Financing for Capital Projects

---

**ORIGIN**

Ongoing Stewardship role of Financial Services and the opportunity to realize a return on cash assets currently being used as a source of bridge financing of Capital Projects.

**RECOMMENDATION**

**It is recommended that:**

- 1) Commencing in the 2005-06 fiscal year that interest be charged for the bridge financing of those Capital Projects that are of benefit to a specific identifiable group or area and which are either partially or fully funded by local improvement charges including those levied as an area rate.
- 2) Commencing in the 2005-06 fiscal year that interest be charged for the bridge financing of Capital Projects that are cost shared and that external cost sharing partners be billed their proportionate share of bridge financing costs. Where interest is not deemed an eligible cost shared expense under the program then the interest cost shall be recovered through local improvement charges where levied.
- 3) The interest rate to be applied to these capital projects be the actual HRM Short Term Investment Rate.

## **BACKGROUND**

It has been an Administrative Policy under the Multi-Year Financial Strategy that the cost of bridge financing not be charged on any Capital Projects. A review of this Policy and recommended changes is the subject of this report. The context for this review is Financial Stewardship to ensure that cash assets are working for the benefit of all of HRM.

HRM provides bridge financing for all Capital Projects from internal cash resources rather than through temporary borrowing, bank lines of credit, etc. The rationale has been that using external sources of financing would only serve to add an interest cost to the HRM Capital Project which in turn would then be financed through the Nova Scotia Municipal Finance Corporation. Additionally, the inclusion of a bridge financing charge can add to the complexity of the planning of individual Capital Projects.

Infrastructure funding from other levels of government as well as large projects such as the Harbour Solutions Project, which is fully financed through user charges and does not rely upon any tax generated funding, have resulted in staff re-evaluating the policy of not charging interest on all capital projects. When interest is not charged on bridge financing for any projects, projects that only benefit an identifiable group or area are subsidized by the general tax rate. This may run contrary to Council's intentions. Moreover, in some cases the project cost sharing agreement may require the HRM to wait a substantial period of time before it can collect cost-sharing on behalf of the local group from external sources. This represents a loss of income to HRM that affects general service delivery in other areas of the organization.

## **DISCUSSION**

### **Status Quo**

The use of internal cash resources for the bridge financing of Capital Projects results in a loss of investment income to the Operating Fund as cash balances available to earn income are reduced (i.e. if the HRM did not have cash on hand it would be required to borrow from a bank, pay interest and then determine whether to charge the interest to the Capital Project). In the case of projects that are debt financed and that are of a general benefit to all, it is quite appropriate both from a purely financial perspective as well as from the standpoint of equity and administrative ease to not charge an interest cost. Increasing the cost of a Capital Project by an interest cost and financing this cost with long term debt would result in current income being gained while there is a greater future cost as this greater debt is repaid with interest at higher long term interest rates. The tax rate of today would gain from an increase in investment income only to pay this

back through increased tax rates of future years through interest and principal payments to bond holders over 10 and 20 year periods. Therefore, in the case of Capital Projects of a general benefit to all taxpayers, the cost of the bridge financing is borne, in staff's view, appropriately by the current year's general tax rate.

### Identifiable Groups

Projects such as those cost shared through Infrastructure Funding have often provided servicing to the benefit of a specific identifiable group or area rather than all taxpayers in general. While the general intent of these Projects has been for the HRM General Rate not to subsidize these Projects, in this situation taxpayers in general are absorbing the cost of bridge financing for the benefit of a specific group. Charging interest on Capital Projects that provide benefit only to a specific group or area will address this inequity and increase income to the Operating Fund for the benefit of all taxpayers while at the same time ensuring that future tax rates are not impacted.

### Cost Shared Projects

Finally, some Capital Projects receive long term financing from sources other than being financed solely through long term debt. Sources such as Municipal, Federal and Provincial Cost Sharing. Project costs are incurred and paid for by HRM well in advance of receipt of payments from cost sharing. The HRM funding partners are seeing their costs reduced because the general taxpayer is absorbing the cost of all of the bridge financing on these cost shared Capital Projects. Charging these Capital Projects the bridge financing cost would ensure that the funding partners cover their fair share of this cost while providing a return on HRM cash assets to benefit all HRM taxpayers. Where funding partners disallow internal interest charges by virtue of an agreement, staff propose there be no interest charge unless the service being provided is being funded in part by an area rate or local improvement charge. In that case the area rate or local improvement charge will cover the full bridge financing cost.

## **BUDGET IMPLICATIONS**

While full information is not available for the 2005/06 budget year, the budget impact based on the Cost Sharing, Local Improvement Charge and Infrastructure funding categories identified in the 2004-05 Capital Budget totaling \$8,436,000 (excluding Harbour Solutions) would result in an increase in Investment Income of approximately \$211,000 at current interest rates assuming bridge financing of this amount for a one year period. This increase in Investment Income will offset the loss due to the reduced cash balances associated with carrying out the Projects.

**FINANCIAL MANAGEMENT POLICIES/BUSINESS PLAN**

This report complies with the Municipality's Multi-Year Financial Strategy, the approved Operating, Capital and Reserve budgets, policies and procedures regarding the withdrawals from the utilization of Capital and Operating reserves, as well as any relevant legislation. It does reflect an amendment to Administrative Policy that was created due to the Multi-Year Financial Strategy.


**ALTERNATIVES**

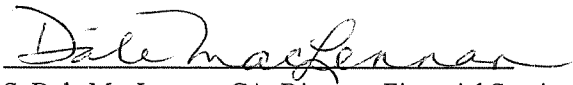
- 1) The current policy of not charging the interest cost of interim financing for all Capital Projects could be maintained.

**ATTACHMENTS**

None.

Additional copies of this report, and information on its status, can be obtained by contacting the Office of the Municipal Clerk at 490-4210, or Fax 490-4208.

Report Prepared by: Derek Tynski, Investment Analyst,  490-6471  
Reg Ridgley, Manager Strategic Capital Project Support, 490-6475

Report Approved by:   
S. Dale MacLennan, CA, Director, Financial Services, 490-6308