Agenda - Executive Policy Committee – March 20, 2008

OPERATING BUDGET REVIEW

Item No. 9 **Special Operating Agency (SOA) Transfer to City and Retained Earnings**
File GL-5.6.1

COMMITTEE RECOMMENDATION:

On October 9, 2007, the Alternate Service Delivery Committee recommended that implementation of the policy with respect to Special Operating Agency Transfers to the City and Retained Earnings be amended by deleting the words “beginning January 1, 2009,” in the first line of Recommendation 1 and substituting therefore the words "commencing January 1, 2008," and referred to the 2008 Budget Review, on the understanding that further changes may be made in the Special Operating Agencies Business Plans to achieve the most favourable results.

DECISION MAKING HISTORY**:**

COMMITTEE RECOMMENDATION:

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On October 2, 2007, the Alternate Service Delivery Committee received as information the report of the Winnipeg Public Service dated September 27, 2007.

RE: Special Operating Agency (SOA) Transfer-to-City and Retained Earnings Policy

FOR SUBMISSION TO: **Alternate Service Delivery Committee**

ORIGINAL REPORT SIGNED BY: Chief Financial Officer

REPORT DATE: September 27, 2007

RECOMMENDATION(s):

It is recommended that:

1. Council adopt the principle that, beginning January 1, 2009, a Special Operating Agency (SOA) will not provide a transfer to the City's General Revenue Fund to the extent that doing so would place it in an accumulated deficit position. (Note: The 2007 Operating Charter of the Winnipeg Fleet Management Agency (WFMA) already provides that WFMA will not make any transfers until it achieves at least a 4:1 debt-to-equity ratio.)
2. Subject to Recommendation 1, Council approve the following transfer guidelines for the Special Operating Agencies:
    - Winnipeg Golf Services (WGS) will transfer a specified sum based on 10% of its projected gross revenues for the year;
    - Winnipeg Parking Authority (WPA) will transfer a specified sum based on 25% of its projected gross revenues for the year; and
    - Once WFMA achieves at least a 4:1 debt to equity ratio it will transfer a specified sum based on the Business Plan of the Agency.
3. That the Operating Charters of the Special Operating Agencies be amended as set out in Appendix 1 to reflect Recommendation 1.
4. The Proper Officers of the City be authorized to do all things necessary to implement the intent of the foregoing.

Report Summary

Key Issues:

- No transfer of funds from any SOA to the City should take place if in doing so it would put the SOA in an accumulated deficit.
- Assuming that they do not have an accumulated deficit, individual SOAs will make transfers to the City and retain some earnings based on formulas appropriate to their lines of business.

- Due to the fact that WFMA has not achieved a 4:1 debt to equity ratio and both WGS and WPA have accumulated deficits, as of 2009 no transfers will be made from these SOAs to the City's General Revenues.
- The matter of the potential transfer distribution to WFMA's customers will be the focus of a subsequent report to Council.
- This transfer Policy is not relevant to Animal Services as it is a tax-supported Agency nor to Glacial Sand and Gravel as its assets have been sold.

Implications of the Recommendation(s):

General Implications

(X) None
() For the organization overall and/or for other departments
( ) For the community and/or organizations external to the City
( ) Involves a multi-year contract

Policy Implications

( ) No
(X) Yes

Comment(s): The proposed transfer Policy will allow the SOAs to achieve a solid financial status before transfers are made to the City. Once an SOA is on a solid financial footing, the transfer guidelines proposed for each SOA will provide an appropriate return to the City while allowing the SOA to retain some earnings for future investment and growth.

Regulatory Implications

(X) None
( ) Eliminates or reduces regulatory impact
( ) Proposes regulatory impact

Environmental Implications

(X) No
( ) Yes

Human Resources Implications

(X) No
( ) Yes

Financial Implications

(X) Within approved current and/or capital budget
( ) Current and/or capital budget adjustment required

Comment(s): While this proposed policy does not affect the 2007 or 2008 budgets, it will have implications for future budgets.

Report

REASON FOR THE REPORT:

The Audit Department's report entitled *Audit of the Special Operating Agencies Initiative Final Report*, which was adopted by Council on March 22, 2006, identified in Recommendation 9 the need for a transfer policy for the Special Operating Agencies (SOA). Specifically, the recommendation stated that:

> 'SOA profitability and accumulated surpluses should be considered when determining ROI transfers to the City'.

HISTORY:

Council has approved five Special Operating Agencies (SOA). These are:

- Animal Services (AS)
- Glacial Sand and Gravel (GSG)
- Winnipeg Golf Services (WGS)
- Winnipeg Fleet Management Agency (WFMA)
- Winnipeg Parking Authority (WPA)

Currently, there are no universal transfer policy guidelines for the SOAs. Winnipeg Fleet Management Agency is the only Agency that has a Council approved transfer guideline that uses a debt to equity ratio based on the industry average. The Winnipeg Parking Authority currently provides an unsustainable flat transfer of $5,300,000 to the City and Winnipeg Golf Services provides $365,844.

DISCUSSION:

This report sets out a Policy for transfers to the City (sometimes referred to as Return on Investment or ROI transfers) and retained earnings for three SOAs (WGS, WFMA, WPA). This Policy is not relevant to Animal Services because that SOA is tax-supported through a grant from the City and is not in a position to make a transfer to the City. Glacial Sand and Gravel has recently sold its Pine Ridge Pit asset and will be dissolving the SOA and transferring the remaining assets to the Public Work Department at the end of 2007.

No Transfers if Accumulated Deficit

Requiring transfers to the City from an SOA when it has an accumulated deficit or when the transfer would drive it into a deficit position effectively requires the SOA to borrow against its assets in order to pay "dividends" to shareholders. This practice is unsustainable in the long run because it does not permit the SOA to achieve financial viability.
With a one year transition period, the new Policy will be that, beginning in January 2009, transfers will only be paid to the extent that doing so will not drive the SOA into an accumulated deficit position. If the SOA cannot pay a transfer due to an accumulated deficit, the SOA must demonstrate in its annual business plan how it will return to a positive (surplus) position.

If this Policy were applied immediately, none of the SOAs would meet their transfer thresholds. The Winnipeg Fleet Management Agency would not meet its 4:1 ratio while the Winnipeg Parking Authority and Winnipeg Golf Services have accumulated deficits. However, this Report is proposing a transition period of one year, so that this policy will only take effect in 2009.

The amendments to the SOAs' Operating Charters necessary to implement this Policy are set out in Appendix 1to this Report.

Individualized SOA Transfer Guidelines

Subject to the Policy set out above, there are different transfer options that could be applied to the SOAs. For example, an SOA could pay a fixed transfer based on a percentage of earnings. Alternatively, it could pay a flat fee, akin to a preferred share approach, in much the same way that the Province of Manitoba SOAs do.

In order to reflect the different lines of business in which the City's SOAs are engaged, the following guidelines, specific to each SOA, are proposed.

Winnipeg Fleet Management Agency (WFMA)

In addition to the policy that no transfer be made that would require the WFMA to run an accumulated deficit, a 2007 Council approved amendment to WFMA's Operating Charter already provides that the Agency will not make any transfers until it achieves at least a 4:1 debt-to-equity ratio (refer to WFMA's 2007 Annual Selection Report, Appendix 1, page 7018, adopted by Council on March 21, 2007).

The debt-to-equity ratio is based on the Risk Management Association's (RMA) Financial Ratio Benchmarks. The Province of Manitoba's Fleet Vehicles Agency SOA uses a fixed transfer approach called 'revenue sharing' which allows the SOA to accumulate retained earnings.

WFMA is converting its City of Winnipeg debt to equity, except for its line of credit/term debt, during 2008. Accordingly, no transfer is projected for 2009 and beyond. WFMA's 2007 adopted business plan, indicates that it will not meet the 4:1 debt to equity threshold beginning in 2009. Therefore, the Agency will not make transfers to the General Revenue Fund for 2009. However, for 2008, WFMA is projected to transfer $912,000 to the General Revenue Fund.

Once WFMA achieves a 4:1 debt to equity ratio, a fixed transfer will be made to the City based on WFMA's Business Plan which may permit the WFMA to retain some of its earnings for future investment.

Winnipeg Golf Services (WGS)

WGS is projecting an accumulated deficit of $2,799,349 in 2008. Because of the one-year transition period for the implementation of the Policy set out in Recommendation 1, a transfer will be paid to the General Revenue Fund in 2008. However, thereafter, WGS is not expected to make a transfer payment until it eliminates its accumulated deficit. It will also be expected to demonstrate through its Business Plan how it will return to a positive position.

Once WGS eliminates its accumulated deficit, the transfer guidelines being proposed will take into account that the golf business is weather dependent in Winnipeg and. recognize the variability of the business from year to year. It should allow the City to share in the years when annual revenues are growing while allowing WGS to retain sufficient earnings to sustain it during low income years.

For this reason, the proposed approach is based on a percentage of projected gross revenues. Specifically, it is proposed that WGS should transfer 10% of its total revenues. Since WGS projects revenues of $3,208,761 for 2008 as contained in WGS's 2007 adopted business plan, this would produce a transfer of $320,876. This is the sum that will be transferred for 2008 during the transition period.

Winnipeg Parking Authority (WPA)

Like WGS, the Winnipeg Parking Authority is currently running an accumulated deficit, projected to be $5,376,000 in 2008. The implications of Recommendation 1 are that, beginning in 2009, WPA will not make transfers to the City until the deficit is eliminated and thereafter will pay transfers only to the extent that the transfers do not create a new deficit.

Once WPA's deficit is eliminated, however, WPA will be able to pay transfers to the City. Transfer guidelines should ensure that the City obtains reasonable revenue from its assets while allowing WPA to retain earnings to permit capital investment in assets such as parking facilities and to undertake long-term initiatives. A recent survey of eight municipal parking authorities revealed transfers based on percentages of gross revenues ranging from 32% for Toronto to 15% for Grand Rapids, Michigan. Winnipeg is currently at 54%.

It is proposed that WPA should pay a transfer based on 25% of projected total revenues for the year. This is roughly the mid-point of the cities surveyed. Based on projected revenues of $14,998,000 for 2008 as contained in WPA's 2007 adopted business plan, this approach would result in a transfer of $3,749,500 in 2008. Due to the transition period proposed for the implementation of Recommendation 1, this is the sum that will be paid in 2008.

Annual Transfer Review Process

The SOAs prepare their annual business plans during the last quarter of the current year for approval by Council ahead of the City's operating budget. The operating budget is adopted no later than March of the following year.

The information in the SOAs' annual business plans regarding the planned transfers to the City are incorporated in the Administration's budget preparation cycle which begins in May. The Business Review and Credit Committee (BRACC), an internal administrative body, reviews the SOAs' third quarter reports to compare their actual revenues against budgets.

If there is a reason that an SOA's revenues are less than budgeted or it incurs an annual operating deficit and it is unable to project retained earnings for the year, then BRACC can recommend that the transfer to the City is adjusted accordingly and that planned activities to return to a positive position are reflected in the SOA's business plan. Or, if an SOA shows a surplus, BRACC can recommend making an extraordinary transfer to the City. Either situation will be reflected in the Administration's operating budget.

Financial Impact Statement **Date:** August 27, 2007

Project Name: **First Year of Program** **2007**

Special Operating Agency Transfer-to-City and Retained Earnings Policy

	2007	2008	2009	2010	2011
Capital					
Capital Expenditures Required	$ -	$ -	$ -	$ -	$ -
Less: Existing Budgeted Costs	-	-	-	-	-
Additional Capital Budget Required	$ -	$ -	$ -	$ -	$ -
Funding Sources:					
Debt - Internal	$ -	$ -	$ -	$ -	$ -
Debt - External	-	-	-	-	-
Grants (Enter Description Here)	-	-	-	-	-
Reserves, Equity, Surplus	-	-	-	-	-
Other - Enter Description Here	-	-	-	-	-
Total Funding	$ -	$ -	$ -	$ -	$ -
Total Additional Capital Budget Required	$ -				
Total Additional Debt Required	$ -				
Current Expenditures/Revenues					
Transfers to the City	$ 7,160,844	$ 4,732,052	$ -	$ -	$ -
Less: Budgeted Transfers to the City	7,160,844	4,732,052	3,820,000	-	-
Net Budget Adjustment Required	$ -	$ -	$ (3,820,000)	$ -	$ -

Additional Comments:

1. The proposed policy does not affect the 2007 and 2008 operating budgets. For 2009, transfers are estimated at $320,000 for Winnipeg Golf Services (WGS) and $3,500,000 for the Winnipeg Parking Authority (WPA), according to SOA's 2007 Council adopted business plans. However, WGS and WPA are likely to be in deficit for 2009, and therefore, may not be making transfers to the City. The worst case scenario is presented in this statement.

2. Winnipeg Fleet Management Agency (WFMA) will not be making a transfer to the City in 2009, as outlined in its Council adopted 2007 business plan.

3. Transfers for years beyond 2009 are to be determined and reported in future business plans.

(Original signed by R. Abeysekera)
Radhika Abeysekera
Manager of Finance & Administration
Corporate Services Dept.

IN PREPARING THIS REPORT THERE WAS:

Internal Consultation With and Concurrence By:

Winnipeg Fleet Management Agency
Winnipeg Golf Services
Winnipeg Parking Authority
Business Review and Credit Committee (BRACC)

External Consultation With:

N/A

THIS REPORT SUBMITTED BY:

Department Internal Services Department
Division
Prepared by: Iain Day, ASD Development Officer
File No.

Appendix 1: Operating Charter Amendments

Special Operating Agency	Addition	Recommendation
WINNIPEG GOLF SERVICES (Adopted by Council on April 24, 2002)	**Section 5: Financial Framework** *5.6 Transfer to the City of Winnipeg*	Recommended language: *The Agency does not provide a transfer to the City's General Revenue Fund if in doing so it will have an accumulated deficit.*
WINNIPEG FLEET MANAGEMENT AGENCY (Adopted by Council on May 28, 2003)	**Section 5: Financial Framework** *5.10.2 Transfer to the City*	Recommended language: *The Agency does not provide a transfer to the City's General Revenue Fund if in doing so it will have an accumulated deficit and a debt to equity ratio of 4:1 or higher.*
WINNIPEG PARKING AUTHORITY (Adopted by Council on October 27, 2004)	**Section 5: Financial Framework** *5.5 Transfer to the City*	Recommended language: *The Agency does not provide a transfer to the City's General Revenue Fund if in doing so it will have an accumulated deficit.*