Municipal debt

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Rendering of the new Clareview Recreation Centre and Library

The City of Edmonton uses debt to finance some large infrastructure projects that will benefit the community over a long time. The City borrows money to finance major capital infrastructure like police stations or fire halls, recreation centres, libraries or new LRT lines.

Why municipal debt is necessary

Using debt to finance large projects allows them to proceed sooner than waiting to save enough in cash or grants to pay for them all at once.

Borrowing allows the City to spread the payments for infrastructure over a portion of the life of the facility. Taxes would jump substantially in any one year if the total costs of an infrastructure project needed to be funded outright in that year.

It is similar to how an individual does not usually pay for a house or a new car in one lump sum. Instead, a mortgage or loan is used to spread payments over a longer time frame.

It is reasonable for a City to borrow money to pay for infrastructure that benefits people over many years, and then pay off the cost over a period of years while the facilities are being used.

For high-priority large projects, borrowing up front may have an added advantage of leveraging dollars from other sources, such as federal or provincial governments or the private sector.

Debt is only used for infrastructure

Just like it is not wise for a household to go into debt to pay for daily, ongoing expenses like buying groceries, a city would be irresponsible if it borrowed money to pay for operating costs like salaries and pension plans of employees. In fact, under provincial law - the Municipal Government Act (MGA) - municipalities cannot borrow for operating expenses; cities can only borrow for infrastructure projects. And cities in Alberta cannot run operating deficits.

The City's Debt Management Fiscal Policy clearly sets out that long-term debt can only be used for large projects with long-term benefits for the community, projects needed to support the growing population, projects that advance the City's priorities, and major rehabilitation of existing assets.

Some examples of projects that have been or will be financed in whole or in part with debt are:

- Walterdale Bridge
- Southeast to West LRT land acquisition
- Multi-purpose recreation centres
- Whitemud Drive/ Quesnell Bridge improvements
- North LRT

THE CITY OF Edmonton

The need for infrastructure spending

Public infrastructure is essential to all residents and businesses in the City of Edmonton. It is critical to the competitiveness of our economy, our quality of life and the delivery of public services. With adequate and properly maintained infrastructure, Edmonton can remain an attractive and cost-effective place to live and do business.

For about a decade from the early 1990s until 2002, the City of Edmonton avoided the use of debt. Unfortunately, this policy meant that much of the infrastructure in the City was not maintained to the level it should have been and demands for new infrastructure to support a booming population were not being fully met.

Although the City avoided debt, it created "infrastructure debt" in which the City fell behind in providing new infrastructure like LRT expansion and recreation facilities for a growing community.

Since 2002, debt is once again a key financing tool for the City to build high priority, major projects.

Fiscal responsibility

When debt is used to finance capital projects, it must be affordable and sustainable. Just like a household should only take on debt that is within the means of that household to repay, a City should only take on debt for major infrastructure projects when the repayment is manageable.

The key to using debt financing is to:

- establish sustainable limits,
- ensure the debt is used only for the right infrastructure projects,
- ensure the debt is structured with sources of repayment in place.

The Alberta Municipal Government Act limits total municipal debt to two times municipal revenues, with debt servicing not to exceed 35% of revenue. The City of Edmonton imposes even more conservative borrowing guidelines through its Debt Management Fiscal Policy (DMFP). It limits total debt servicing to 22% of annual City revenues. The City of Edmonton's debt at the beginning of 2013 was $2.2 billion. Under the Municipal Government Act, the City could borrow as much as $4.2 billion – which means the City is only at 53% of the debt limit set by the Province. It could borrow $2 billion more than it has.

As we pay off debt, our debt room (the amount of money we can borrow for future projects) will grow in 2017 through to 2021.

Interest rates and terms

Edmonton is able to borrow money at a rate of interest below what is available to citizens, and the City can lock in rates over the duration of the loan period. Currently, interest rates on the City's debt range from as low as 1.59% for 5 year terms to 3.27% for 25 year terms – still a very low rate.

Debt vs. deficits

There is some confusion about the difference between debt and deficits. "Debt" occurs when money is borrowed and must be repaid in the future. The amount owing is the debt. A "deficit" is when a government (or any organization) does not take in enough revenue to meet its operating expenses in a given year.

The federal and provincial governments sometimes run "deficits" on purpose, borrowing money to meet their expenses in the belief that future revenues will be higher and will allow them to repay the accumulated debts. However under the Municipal Government Act, the City of Edmonton *cannot borrow for operating expenses and cannot plan to run an operating deficit*. If a deficit does occur at the end of a year due to emergencies or unplanned costs, the City must pay it off. That's why the City has a Financial Stabilization Reserve to fund unforeseen deficits. The FSR is built up in years when there is a surplus (or when costs of operations turn out to be less than actual revenue).