
2023 CAPITAL BUDGET BRIEFING NOTE

Cost Escalation and Supply Chain Impacts on the Corporate Real Estate Management SOGR Backlog

Issue/Background:

At its meeting on January 13th, 2023, the Budget Committee requested a briefing note from the Executive Director, Corporate Real Estate Management (CREM) on detailed estimates for the additional expected costs associated with the ongoing cost escalations and supply chain issues highlighted by the department which have not yet been factored into the State of Good Repair (SOGR) backlog.

Key Points:

- CREM leads life cycle asset management and improvements at 478 City-owned facilities with an approximate replacement value of \$5.9 billion, covering more than 12.0 million square feet. Approximately 20% of the City-wide portfolio of facilities are under direct capital management of CREM.
- Page 17 of the [2023 Budget Notes for CREM](#) outlines the total SOGR funding and backlog within the CREM portfolio. Overall, the backlog is increasing from 17.6% of replacement value in 2023 to 21.9% by 2032.
- There are various factors that are contributing to this increase, including an annual investment in SOGR for aging City facilities at a rate of 1% compared to an industry standard of 2% to 4%, reduction in recent SOGR funding to address COVID-19 funding support shortfalls from the federal and provincial governments, and resource constraints and prioritization experienced in recent years resulting in the need to re-align SOGR cash flows to reflect the Division's capacity to deliver projects.
- An annual escalation factor based on long-term historical averages is included in the 10 year SOGR backlog.
- Since 2020, market conditions, such as supply chain constraints and other macroeconomic factors have led to cost escalation of over 10-15% per annum in the construction industry.
- Market forecasts, provided by cost consultants in the construction industry, indicate higher than normal cost escalations will continue in the short-term, but at a reduced rate, returning to the historical norms within the next 3 years.

- There are various macroeconomic factors that could influence market conditions in any given year. Given this uncertainty it is prudent to use long-term historical averages to forecast the 10 year outlook for SOGR backlog.

Asset management plans and strategies:

- The SOGR backlog also does not reflect the impacts of strategies that are being put in place to address the backlog challenges.
- Through two priority actions initiated in 2022, the CREM Division has a plan to address the growing backlog while maintaining existing facilities in a state of good repair, operational and safe for City and public use.
 - Corporate Real Estate Management is developing and implementing industry standard Asset Management plans, programs and practices. This includes strategic approaches to addressing the growing backlog and implementing the appropriate preventative maintenance programs to reduce the overall cost of ownership of assets, improve performance and reduce failure, downtime and major maintenance investments.
 - The rationalization of office space supported through the ModernTO Workplace Modernization Program will reduce the overall size of the building portfolio, and as a result reduce the need to invest in state of good repair backlog across facilities that will no longer be used for City purposes. This programmatic approach, being led by CreateTO through its strategic portfolio reviews of all City asset types, will be an ongoing initiative to rationalize and optimize the City's real estate portfolio as part of the City-Wide Real Estate Model.
- In addition CREM will work with the Financial Planning Division as part of a review SOGR challenges and return with a strategy and opportunities aimed at reducing SOGR backlog through the 2024 budget process.

Prepared by: Marco Cuoco, Director, Business Management, Corporate Real Estate Management Division, 416-397-7338, marco.cuoco@toronto.ca

Further information: Patrick Matozzo, Executive Director, Corporate Real Estate Management Division, 416-392-9158, patrick.matozzo@toronto.ca

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