HALIFAX

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Item No. 03
Committee of The Whole
December 14, 2016

TO: Mayor Savage and Members of Halifax Regional Council

Original Signed by

SUBMITTED BY:

Jacques Dubé, Chief Administrative Officer

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Jane Fraser, Acting Deputy Chief Administrative Officer

DATE: December 1, 2016

SUBJECT: Fiscal Framework

ORIGIN

The fiscal direction from Council for the 2017-18 and 2018-19 Budget and Business Plans needs to be established.

LEGISLATIVE AUTHORITY

Halifax Charter, section 35 (1) The Chief Administrative Officer shall (B) ensure that an annual budget is prepared and submitted to the Council.

RECOMMENDATION

It is recommended that staff develop the multi-year operating budgets for 2017-2018 and 2018-2019 according to Council's approved priorities, and preliminary fiscal direction, including:

- Maintaining the appropriate level of existing services with the addition of the new services previously approved by Council;
- a stable capital budget that maintains state of good repair while also funding growth related issues and service improvements;
- a responsible and declining debt position;
- appropriate reserve balances that allow for risk mitigation, future obligations and opportunities;
- alignment of the current average tax bill for residential homes and commercial properties with all relative economic indicators.

BACKGROUND

In February of 2016 Regional Council directed staff to undertake

> *… in 2017-2018 and the following years, a much broader view that looks at the underlying fiscal and economic assumptions and critical key decisions such as the level of the overall capital budget, debt, tax levels, reserves and the capacity to undertake service enhancements.*

Staff have completed some of the key processes that will help build a much more financially sustainable approach. Part of this is a new multi-year approach to budgeting. For the first time, staff intend to present to Council a two year budget. The first year (2017-2018) will be the formal approved budget. The second year (2018-2019) will be approved in principle and used throughout 2017-2018 as a planning document. Staff is also preparing longer term fiscal direction for 2019-2020 and 2020-2021.

As part of this new approach, Staff is currently in the initial stages of planning for Years 1 through 4. As part of that process, Council has already engaged in a dialogue on priorities and outcomes. Commencing January 25th, 2017 and continuing through into March of 2017, Council will begin the review of individual budgets and plans for the upcoming fiscal year. The first stage of this process, however, consists of providing broad direction to staff on the underlying assumptions for taxation and fiscal items. These assumptions, in turn, will influence the available funds for each of the services and projects the municipality is able to undertake in 2017-18 and future years.

DISCUSSION

Preparing and finalizing a budget for HRM is an extensive exercise which includes many iterative steps. There is tremendous demand for new and improved services; the maintenance of existing services; extension of current services to new homes and businesses; and, the ongoing maintenance of $3.4 billion in municipal assets. Balanced against this is the need to set appropriate tax levies on homeowners, businesses and others. The revenues from these rates allow for the provision of these services. Regardless, the proposed tax levy must be balanced against the value to society of those services, the ability of taxpayers to pay for those items, and the broad competitiveness that the mix of services and taxes will support.

<u>Four Critical Influences and Seven Key Council Decisions</u>:

As directed by Council, staff are preparing for a longer term fiscal approach that integrates key items in the budget process. As such, Staff have identified four critical influences that affect the municipality's fiscal situation. These four key influences are:

1. Operating Budget,
2. Net Capital Budget,
3. Tax Supported Debt, and,
4. Reserves (Net Obligations)

Within these four critical influences there are seven key decisions that Council will have to provide direction on to staff:

Operating Budget

1. Taxes – Should taxes rise, fall or stay the same?
2. Services (Existing) – How can value be optimized?
3. Services (New) – Will new services be funded?

Capital Budget

4. How much should be invested in State of Good Repair, Growth and Service Improvements?
5. Capital from Operating – How much should HRM pay down on the Capital Budget?

Tax Supported Debt

6. What level of debt does HRM wish to approve?

Reserves

7. What reserve balances does HRM expect?

Economic and Financial Assumptions

The HRM economy is generally a stable economy that shows consistent yet moderate growth. That growth is supported by a mixture of a strong public sector employment and by a considerable presence of finance, insurance and real estate sectors. Staff consulted with the Halifax Partnership in determining a series of assumptions for use in fiscal scenarios.

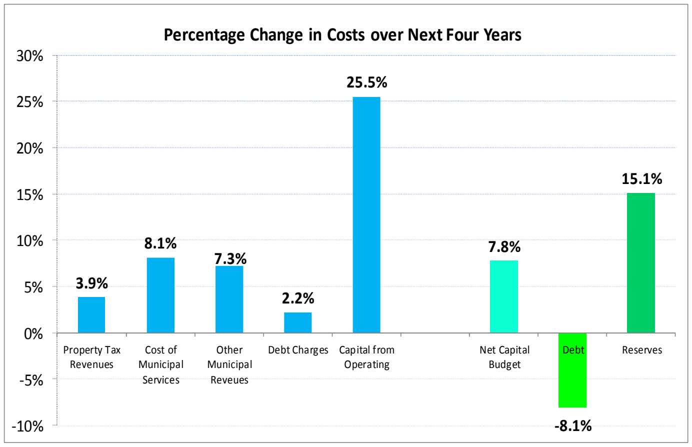
The Partnership has concluded that HRM's economy is growing quickly, with very positive forecasts coming from organizations such as the Conference Board of Canada and local experts at Canmac Economics. Both forecasters predict a high level of GDP growth for the city this year, with 2.6% to 2.9% growth in 2016. They also predict 2.5% to 3.2% growth in 2017 as activity at the shipyard continues to ramp up, and both wholesale and retail spending spur economic activity. While these forecasters differ in the longer term predictions, there is consensus that this will be a strong year for HRM's economy, with strong growth next year as well.

	Year 1	**Year 2**	**Year 3**	**Year 4**
	2017-18	2018-19	2019-20	2020-21
Real Gross Domestic Product (GDP)	2.5%	1.7%	1.7%	1.2%
Personal Income per Capita	45,207	46,121	47,286	48,449
- Percent Change	2.2%	2.0%	2.5%	2.5%
Consumer Price Index	1.7%	1.9%	2.2%	2.0%
Population (000)	428	433	438	442
Dwelling Units	195,100	196,954	198,782	200,627
Dwelling Units %	1.0%	1.0%	0.9%	0.9%

In order to help prepare a base case scenario, staff have made a number of assumptions related to other factors. They have assumed that the average taxes for residential and commercial taxpayers remain constant, that Tax Supported Debt continues to decline and Capital from Operating to increase as per Council's approach to those targets.

The Base Case Scenario

Based on the initial assumptions, staff projected a base case scenario for the next four years. This scenario includes the above economic and financial assumptions as well as the estimated cost of service adjustments already approved by Council. The Base Case scenario shows a $12m shortfall in the first year which, without corrective actions, widens to $63m by year 4. When reviewing the individual cost drivers the results are not surprising. The growth in tax revenues is considerably less than the expected cost of services.



Base Case Scenario - Taxes Flat, Expenses Rise with Inflation and Demographics

	Base Year 2016-17	Year 1 2017-18	Year 2 2018-19	Year 3 2019-20	Year 4 2020-21
Operating Budget Gap (Millions)	**$0**	**$12**	**$28**	**$47**	**$63**
Average Property Tax Bill	**$1,835**	**$1,835**	**$1,835**	**$1,835**	**$1,835**
Property Tax Revenues	**$517m**	**$522m**	**$527m**	**$531m**	**$536m**
Existing and New Homes and Businesses	516.5	521.9	526.7	531.3	536.5
Tax Increase/Decrease	0.0	0.0	0.0	0.0	0.0
Services provided	**$452m**	**$463m**	**$472m**	**$481m**	**$489m**
Exisiting Services (net cost)	452.2	457.3	462.0	467.3	472.1
New or Expanded Services	0.0	5.3	9.7	13.9	17.0
Fiscal Items	**$64m**	**$71m**	**$83m**	**$97m**	**$110m**
Debt Charges - to repay debt (Capital Budget)	54.2	52.2	54.0	55.7	55.4
Capital from Operating - for the Capital Budget	41.3	43.7	46.3	48.9	51.8
Reserves - for risk, opportunities, obligations	22.1	22.3	22.5	22.7	22.9
Other expenses and revenues (net)	-53.3	-47.0	-39.5	-30.6	-20.1
Net Capital Budget (Millions)	**$100**	**$97**	**$101**	**$105**	**$108**
Debt (Millions)	**$250.9**	**$245.8**	**$240.7**	**$235.6**	**$230.6**
Per Dwelling	**$1,299**	**$1,260**	**$1,222**	**$1,185**	**$1,149**
Debt Ratio (Tax Supported)	**5.9%**	**5.7%**	**5.9%**	**6.2%**	**6.1%**
Reserves (Millions)	**$95.3**	**$118.3**	**$117.1**	**$114.4**	**$109.8**

Note: 1996-97 Net Capital Budget ($100m) includes additional Debt, Capital from Operating and Gas Tax funds. Gross Capital Budget ($198m) also includes $98m in cost sharing, infrastructure funds and reserves.

This is essentially an assumption driven framework that helps plan sustainable decisions for the next four years. As direction is given and assumptions are revised due to new information, these gaps will start to close and the full implications will become much clearer.

Three Scenarios

There are a wide variety of possible scenarios that would balance the provision of services with the property taxes and fees paid by the public.

One scenario would be to focus on the capital budget. Much of the Capital Budget is eventually funded through taxation either upfront through the use of Capital from Operating, or after construction through the repayment of principle and interest. In addition, new assets tend to come with additional operating costs. To balance over four years would require substantial reductions in the capital budget that would significantly constrain capital and impact the regional economy.

A second approach would be to focus on reducing the direct cost of services in the operating budget. There is considerable cost pressure on existing budgets. These pressures come from inflation, the increasing number of homes to service and the addition of new or expanded services. While efficiencies, cost improvements and re-priorizations are to be expected, they are unlikely to offset the cost pressures in many services

The recommended approach is to use a combination of changes to taxation, capital budget and services in order to move towards a more sustainable financial position. Rather than holding the average tax bill flat (essentially a reduction in real terms), taxes should rise by 1.8% and 1.6% in years 1 and 2 of the Plan. This is $34 on the average single family home in 2017-2018 and $103 over four years. These changes are comparable to inflation and slightly below predicted personal income growth (per the Conference Board of Canada). In years 3 and 4 increases would be moderated. At the same time, increases in the cost of services and the Capital Budget would have to be constrained otherwise tax changes would need to be higher.

FINANCIAL IMPLICATIONS

There are no immediate financial implications associated with this recommendation.

RISK CONSIDERATION

Risks related to the recommendations in this Report include changes in the underlying economic assumptions as well as assumptions as to the value of the final assessment roll. The risks can be better defined and managed as the two year budget is developed. Similar risks will also be present in most of the alternatives to the recommendations.

COMMUNITY ENGAGEMENT

Budget Consultations will consist of an on-line balance-the-budget tool (the “budget allocator”) as well as an opportunity for the Public to attend the Business Unit draft budget presentations to Committee of the Whole, and ask questions afterwards.

ENVIRONMENTAL IMPLICATIONS

None.

ALTERNATIVES

None.

ATTACHMENTS

None.

A copy of this report can be obtained online at http://www.halifax.ca/council/agendasc/cagenda.php then choose the appropriate meeting date, or by contacting the Office of the Municipal Clerk at 902.490.4210, or Fax 902.490.4208.

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