HALIFAX

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Item No. 5
Committee of The Whole
November 27, 2018

TO: Mayor Savage and Members of Halifax Regional Council

SUBMITTED BY: Original Signed by

Jacques Dubé, Chief Administrative Officer

DATE: November 20, 2018

SUBJECT: Fiscal Framework

ORIGIN

The fiscal direction from Council for the 2019-20 and 2020-21 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 Halifax Regional Council direct staff to develop the 2019-2020 Budget and 2020-21 Budget in Principle 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 three-year capital budget that recapitalizes assets, funds growth related issues and is balanced to the fiscal framework;
- a responsible debt position;
- appropriate reserve balances that allow for risk mitigation, future obligations, and opportunities; and,
- alignment of the current average tax bill for residential homes and commercial properties under two scenarios:
  a) 2.1% increase for 2019-20;
  b) 2.9% increase for 2019-20.

BACKGROUND

In 2017-18 Council initiated its first two-year budget cycle. That cycle ended with the 2018-19 Budget. Consequently, 2019-20 is the start of the next two-year budget cycle. The first year (2019-2020) will be the formally approved budget. The second year (2020-2021) will be approved in principle and used throughout 2019-2020 as a planning document. Staff is also preparing longer term fiscal direction for Year 3 (2021-2022) and Year 4 (2022-2023).

As part of that process, Council has already started a dialogue on priorities and outcomes. The Three-Year Capital Budget will be presented to Council on December 4, 2018. Commencing January 16, 2019 and continuing through into February 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 2019-20 and future years.

DISCUSSION

Preparing and finalizing a budget for Halifax 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 $3.6 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. <u>Taxes</u> – Should taxes rise, fall or stay the same?
2. <u>Services (Existing)</u> – How can value be optimized?
3. <u>Services (New)</u> – 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 a small open economy that shows consistent yet moderate growth. That growth is supported by a mixture of strong public-sector employment and by a considerable presence of finance, insurance, and real estate activity Staff consulted with the Halifax Partnership in determining a series of assumptions for use in fiscal scenarios and has used data from the Conference Board of Canada and Canmac Economics.

HRM's economy is growing, with positive forecasts for Real GDP and income growth of 2.5%. Inflation is stable at 2.1%. The population and number of dwelling units are growing steadily over the next four years.

	Year 1 2019-20	Year 2 2020-21	Year 3 2021-22	Year 4 2022-23
Real Gross Domestic Product (RDP)	19,234	19,518	19,855	20,199
Personal Income per Capita	46,179	47,350	48,661	50,032
- Percent Change	2.5%	2.5%	2.8%	2.8%
Inflation (CPI)	2.1%	2.2%	2.2%	2.2%
Population (000)	444.0	449.0	455.0	460.0
Dwelling Units	197,887	200,199	202,464	204,706
- Percent Change	1.2%	1.2%	1.1%	1.1%

To prepare a base case scenario, staff has made several 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 that Capital from Operating increases as per Council's approach to those targets. Included in the forecast are the cost of wage settlements and higher fuel prices.

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 $15m shortfall in the first year, which without corrective actions, widens to $48m by year 4. The growth in tax revenues is considerably less than the expected cost of services. The key factors in the forecast are:

- **New or adjusted services (additional RCMP, Ferry service, cost of operating new assets) will cost $7.9m**. Many of these services are provided to deal with the growing population across the region;

- There is **considerable wage pressure, resulting in an increase of $15m** attributed to collective agreements, step positions, an additional 2 work days in the year as well as reclasses and other adjustments. (For clarity, there is another $2.6m in compensation that is part of the $7.9m in new services);

- **Fuel prices have increased significantly since the 2018-19 budget** was established, adding $3m in cost to operate vehicles such as police cars, fire engines, and transit buses, as well as heating municipal facilities.

- While the economy is strong, the **commercial assessment values are at the low point of their cycle and are growing only modestly.** Hence, property tax revenues from new growth are minimal, providing only $3m.

Options

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

One approach is to reduce municipal services, and hence their costs 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-prioritizations are to be expected, they are unlikely to offset the rising cost pressures in many services.

Cost pressures on existing services in 2019-20 average 3.3%. The greatest cost pressure is on salaries and fuel. Both are influenced by the underlying economics of inflation and rising incomes. Other cost pressures are currently minimal or have been absorbed across the organization. Savings have occurred in debt charges ($3m). Staff have also identified individual savings across the organization as well as areas where revenue forecasts can be adjusted upward.

However, the Municipality is heavily dependent upon property tax revenues to finance its operations. Property tax (along with Payments in Lieu and area rates) funds almost 80% of operations. If costs continue to rise and assessment is flat the municipal budget cannot be sustained while average taxes remain flat. Under these circumstances, the only options for the municipality are to either reduce services or increase taxes. Unless services are constrained, tax increases that are consistent with the rates of inflation and income growth are inevitable.

Rather than holding the average tax bill flat (essentially a reduction in real terms), taxes should rise by 2.9% and 2.2% in years 1 and 2 of the Plan. This is $56 on the average single-family home in 2019-2020 and $44 in Year Two. These changes are slightly higher than inflation and but comparable to personal income growth. In years 3 and 4 increases would be consistent with inflation and would provide for a more sustainable financial path. In themselves, these rate changes would not allow for additional service expansion above that already approved by Regional Council.

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

A Citizen Survey has been conducted to gauge citizen attitudes towards services and taxes. Budget Consultations will include 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

1. Presentation - Fiscal Framework 2019 to 2023

A copy of this report can be obtained online at halifax.ca or by contacting the Office of the Municipal Clerk at 902.490.4210.

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