What is the Long-Range Financial Plan and why do we need it?

The City of Ottawa’s Long-Range Financial Plan III (LRFP III) is the third long-range financial planning document developed since amalgamation and it builds on information provided in previous versions. This wide-ranging document provides a financial profile of the City’s expenditures, revenues, assets and liabilities and a 10-year forecast of capital needs along with a four-year term of Council operating forecast.

LRFP III makes Ottawa’s current financial picture clear and accessible to residents, businesses and elected officials. It provides elected officials with essential information for making decisions that are both financially responsible and responsive to community needs. It provides a comprehensive review of the City’s financial conditions that will also help frame discussions with other levels of government and the community. In addition, it focuses on challenges to the City’s financial sustainability and identifies some strategies as options for consideration in order to achieve long-term financial sustainability.

The Local Government Association of Australia defines financial sustainability within the municipal government context as:

“…a government’s ability to manage its finances so it can meet its spending commitments, both now and in the future. It ensures future generations of taxpayers do not face an unmanageable bill for government services provided to the current generation.”

Using this definition, a municipality’s long-term financial performance is only sustainable when planned long-term service and infrastructure levels and standards can be met without resorting to unplanned increases in rates or disruptive cuts to services.

The City of Ottawa is a complex service delivery organization with approximately 17,000 employees, a $2.2 billion budget, and responsibility for managing over $26 billion in public assets. It is an important economic generator in the local economy, supporting approximately 7,000 local vendors and adding $1.5 billion to Ottawa’s economy every year. It also has more than 100 different public services, many of which are either provincially mandated or provincially and/or federally regulated.

As a corporation, the City’s approach to managing its finances, including long-range financial planning, has earned the respect of independent financial agencies. Moody’s Investors Service has awarded the City an Aaa credit rating for the sixth year in a row, noting: “The City has displayed strong financial performance over the past several years, reflecting strict fiscal discipline and a commitment to long-range financial planning.”

The core business of the City of Ottawa is to deliver important services that enhance Ottawa’s quality of life on a daily basis. The City also builds and maintains extensive and critical public infrastructure like roads, bridges, sidewalks, community centres, swimming pools, sewers and watermains.

* Moody’s Investors Service analysis of the City of Ottawa, July 2006.*
In 2005, Mercer International rated Ottawa 20th in the world for quality of life, ahead of Montréal, Calgary and most American cities, and ranked it 122nd out of 144 cities for cost of living, making it less expensive to live in than Toronto, Vancouver, Calgary and Montréal.

The City is doing well and yet, as this document shows, there are challenges ahead if we are to maintain our current standard of living. Canadian cities simply do not have the financial tools to meet all of their responsibilities. While cities deliver most of the services and build most of the infrastructure that support economic growth, they receive almost none of the tax revenues generated by that growth. Ontario municipalities are further disadvantaged by having to deliver and fund health and social service programs.

Ontario cities must fund services with only three main tools under their control: property taxes, user fees and development charges. Experts agree that, although the federal and provincial governments have begun to provide municipalities with new funding streams by sharing a small portion of their gas taxes, funding from the federal and provincial governments remains ad hoc and inadequate. Municipal finance experts Richard Bird and Enid Slack wrote in May, 2006:

“Big cities…are economically critical to the country’s success …[but] they are, in a sense, nobody’s business. We suggest…that this situation cannot continue. Either someone ‘up there’ in the constitutionally ‘real’ federal and especially provincial spheres has to begin to take cities seriously, or the good life [currently enjoyed] in Canada’s large cities may…become considerably less good…[It] is very likely that …Canadian cities are, if not over the ‘fiscal hill’, at least close to the top.”

The City of Ottawa is working with other large cities in Canada to try to change the municipal fiscal imbalance, and strategies aimed at that objective are presented in this document. In the meantime, Ottawa must continue to succeed within the existing framework until real change occurs at other levels of government.

The challenge of preserving Ottawa’s existing quality of life requires elected officials to work with residents to find the right balance between maintaining existing services and infrastructure for our growing city, providing services mandated by the Province, and enhancing services to meet emerging community needs, all with the limited number of existing funding tools available to Ontario municipalities.

Elected officials and residents need information contained in LRFP III in order to be able to make informed decisions about City services, service levels and how services will be funded – decisions that touch everyone’s lives and have long-term impact. A brief summary of this information follows.

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Ottawa has a strong economy that is growing.

Ottawa has a strong and stable economy with thriving communities, low unemployment, relatively high wages and continuous population growth. The foundations of the economy are strong and Ottawa is well positioned to keep enjoying a generally high standard of living. The population is over 870,000 and our $40 billion Gross Domestic Product keeps increasing. While the federal government and the high-tech sector are the main employers, there are more than 25,000 other employers in the City, providing more that 500,000 jobs.

Changing demographics mean changing municipal service needs.

Like other North American cities, the demographic make-up of the City is changing. The population is aging and in every age group other than people over 55, the numbers are declining as a percentage of the population. Like many other large Canadian cities, Ottawa has benefited from sustained growth in immigration. Recent immigrants – i.e., those who have settled here in the past 10 years – make up 6.8% of the population. In fact, 70,500 recent immigrants now live in Ottawa, the fourth highest concentration in the country. These demographic changes are exerting pressure on the City to provide different services that reflect changing needs.

The City’s operating spending is in line with other Ontario cities.

In 2001, the amalgamated City of Ottawa was created to provide streamlined governance and more efficient, cost-effective delivery of municipal services. This has been achieved with over $101 million in permanent savings. The City was able to achieve tax savings by focusing on finding major efficiencies without affecting service levels. During the first three years after amalgamation, the City was able to maintain existing property tax levels while other municipalities across Ontario and the rest of Canada saw their taxes increase.

Comparison of peer-to-peer city spending (on a per-household basis) between Ottawa, Toronto and a seven-city average of Ontario municipalities (Peel, York, Halton, Niagara, Durham, Hamilton and London) shows that overall spending in Ottawa is only 4% higher than for the seven-city average and 30% less than in Toronto.

Ottawa’s spending was comparable to or below the seven-city average for more than half of the 21 services reviewed. Spending was higher than the seven-city average for big-city services such as social assistance, social housing and transit.

However, Ottawa spends the same or less per household than Toronto to provide those big-city services. In fact, Ottawa spends less for over three-quarters of the services when compared to Toronto.

Ottawa spends more on providing winter services such as road and sidewalk snow clearing and salting than Toronto or the other seven cities because of harsher winters and the larger geographic size of the City. Ottawa is still growing and must pay for
programs and services in new communities. Toronto does not face these pressures because the city infrastructure and services have already been built.

As with other municipalities, the cost of goods and services needed to run City operations has outpaced increases in the Consumer Price Index (CPI). The bulk of budget pressures large municipalities face every year are made up of cost increases above CPI for employee compensation, energy, fuel, steel, concrete and many other goods and services.

In the past six years, the City has been able to manage these pressures as a result of savings from amalgamation and the implementation of efficiency programs and service reductions. The City remains committed to continuously improving efficiency and obtaining best value for purchased goods and services through competition. However, these savings will be much lower than those achieved immediately following amalgamation.

Over the next four years, the cost of providing existing services is projected to increase from $55 million to $61 million per year.

**Provincial social programs should not be on the tax bill.**

Ontario is the only province in Canada to fund more than $3.5 billion annually of primarily social programs, like social services, social housing and public health from property taxes. These programs are controlled by the Province and are funded from a combination of property taxation and provincial subsidy. As the Province controls service levels and overall cost of these programs, Council cannot change the amount that must be raised from property taxes.

Estimated requirements for social programs over the next four years are forecasted to increase property taxes by approximately 0.7% annually, representing a $6 to $8 million increase per year.

If the Province funded all of its mandated cost-shared programs, the average urban residential household in Ottawa would pay $670 less in property taxes per year.

Ontario municipalities have argued for many years that income redistribution programs, such as social assistance, should not be funded from property tax – a regressive tax that does not reflect the income level of a property owner. Instead, it would be more appropriate to fund these programs from provincial income taxes.

**The Province is not adequately funding its share of cost-shared programs.**

Moving beyond the argument around which level of government should fund a program, the level of funding received by municipalities must be examined. There are significant funding gaps in many provincially legislated and cost-shared programs. In this context, a gap is defined as the difference between the funding set by cost-sharing agreements, and the actual amount the Province provides the City.
For 2006, the funding gap for such programs totals about $16 million. There is no other choice than to fund the gap from Ottawa property taxes as the City is mandated to provide these programs at the level of service determined by the Province.

**Provincial funding inequities favour Toronto taxpayers over Ottawa taxpayers.**

Toronto receives grants and subsidies from the Province and other municipalities that reduce its social assistance program costs by 65%. Ottawa’s share only reduces program costs by 55%. In 2006, the owner of an average Ottawa home paid $2,548 in municipal property taxes, excluding provincial education tax. The owner of an average home in Toronto paid $2,093 or $455 less. Ottawa residents also pay an increasing share of education taxes, an additional $28 million since 2001.

The peer-to-peer spending comparison showed that Toronto spends more per household on social assistance than Ottawa. It also showed that the two cities require comparable amounts of tax per household for social assistance. Toronto’s high social assistance costs have been recognized by the Province, and a program was put in place requiring neighbouring municipalities to contribute to Toronto’s social service costs. In 2005, this equalization formula helped Toronto taxpayers save $189 million in property taxes.

Ottawa’s social assistance and social housing costs are higher than the provincial average, but Ottawa does not have the benefit of being included in any type of pooling. If Ottawa were to be included in the same pooling formula, Ottawa residents would pay $53 million less in taxes.

The Ontario Municipal Partnership Fund (OMPF) provides grants to municipalities with high social costs. In 2006, Ottawa will receive $6 million in OMPF grants, or approximately 3% of social program expenditures. Toronto will receive $34.9 million in OMPF grants, representing 6% of its social program costs. If Ottawa residents were treated the same as those in Toronto, Ottawa’s grant would be $12 million.

**Managing compensation costs is one of the most important issues for large municipalities.**

Approximately 95% of the City’s workforce is unionized, and arbitrated wage decisions are often based on awards made in the Greater Toronto Area, which raises costs to the highest level for all municipalities, regardless of work environment. This makes controlling compensation costs a major challenge for all municipalities.

A review of compensation by Mercer Human Resource Consulting showed that unionized City positions are paid the same as those in other municipalities and the same or slightly better than positions in the private sector. The same is not true for many specialized technical positions and many management positions, which are paid below the median rates for the private sector.
The City is managing compensation costs by ensuring that there are tight controls on staffing levels. At amalgamation, there were 12,786 Full-Time Equivalent (FTE) positions. Through reductions from amalgamation, the Universal Program Review and the 2006 budget, 1,236 FTEs have been eliminated.

There has been an overall net increase of 682 FTEs since amalgamation (including 306 more police FTEs), or 5.3% more than in 2000. However, it is important to note that the ratio of staff per thousand residents has declined since 2001 from 16.2 staff per thousand residents to 15.5 staff per thousand. There are 367 fewer administrative and support staff than in 2000 and 743 more operational or front-line service staff.

**Ottawa taxes are similar to other large Ontario cities – cities need new revenue sources other than taxation.**

Ottawa taxes have increased on average by 2% per year over the last six years – less than any other major municipality in Ontario. Despite lower annual increases, Ottawa property taxes are among the highest in Canada largely because Ontario is the highest property tax jurisdiction in the country due to social program funding requirements on the property tax bill.

The Province provides annual property assessments through the Municipal Property Assessment Corporation (MPAC). Ottawa has high property values and some neighbourhoods have seen large increases in the last two re-assessments. Municipalities need tools to mitigate the impact of these changes.

The Province sets the rate of tax increase based on re-assessment of commercial, multi-residential and industrial properties. The phase in of tax increases in these classes has resulted in taxation inequities. Cities need more control over the implementation of changes that result from re-assessment.

Economic and policy experts agree that Canada’s cities lack the legislative and financial tools needed to adequately fund the services and programs they must deliver. If the municipal fiscal imbalance is not addressed soon, Canadian cities will not be able to continue to fund existing services and infrastructure. Rectifying this situation is essential for Canada’s economic prosperity.

Municipalities fund operations through property taxes, grants from federal and provincial governments, user fees, water and sewer rates and transfers from City reserve funds. However, none of these sources of revenue are growing at adequate rates to fund the annual growth in expenditures. Therefore, the City must look beyond taxation and user fees to other sources of revenue.
Canadian cities are having difficulty finding adequate funding for infrastructure projects.

The City has responsibility for maintaining a variety of major types of infrastructure, with an approximate replacement value of $26.4 billion. These assets include roads, water and sewer networks, public transit, buildings, buses and paramedic vehicles. The City budget classifies infrastructure projects into three categories: renewal of City assets, growth, and strategic initiatives.

Historically, there has been a trend to defer capital rehabilitation and renewal to meet the pressure for balanced municipal budgets without large tax increases. The May 2006 research report on municipal finances prepared by Standard & Poor’s, reported that:

“Municipal infrastructure renewal is now an important national issue. Municipal infrastructure deficiencies are typically related to water, sewer, road and transit networks, and municipal building and facilities. Estimates of the total national municipal deficiency, ranging from C$60 billion to C$120 billion, have been frequently reported.”

Over the next 10 years, the “funding gap” to address the capital renewal requirements, which are funded from taxation, is projected to be $1.1 billion.

Liabilities incurred today must start to be funded by today’s taxpayers.

Financial sustainability means that future generations will not be burdened with paying for services that today’s generation of taxpayers enjoy. The City incurs expenses that do not have to be immediately paid (liabilities). For instance, the City will face future budget pressures when existing landfills are full and must be closed and maintained. Pressures will also mount as the City workforce ages and post-employment or post-retirement benefits start to be paid out in larger quantities.

Prudent and sustainable financial management strategies are needed to ensure future generations are not required to absorb a disproportionate share of these costs.

Provincial programs should not be on the property tax bill:

- Request provincial funding for provincially mandated programs that live up to cost-sharing agreements.
- Lobby the Province to remove social programs from the property tax bill.
- Work with the Province to align program accountability and responsibility with funding responsibility.

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• Request the Province to allow provincially mandated programs to be shown separately on the tax bill.

• Use increases in provincial program funding to reduce taxes, not to enhance the level of service provided.

Fix funding inequities in provincial grant allocations for social services:

• Provide detailed input for the Provincial-Municipal Fiscal and Service Delivery Review being conducted over the next 18 months.

• Lobby the Province to provide Ottawa with the same level of grant allocation for social programs as are provided to Toronto.

Fix the re-assessment and tax systems to restore fairness:

• Work with the Province on the review of MPAC over the next two years to reduce the frequency of re-assessments and allow municipalities to phase in changes.

• Request provincial changes to the tax system to give more tax policy discretion to councils to reduce the negative impact of capping and tax shifting.

• Request the Province to either remove education taxes from the property tax bill or establish the amount to be collected rather than the education tax rate.

Better manage compensation and the cost of purchased goods and services:

• Work with large municipalities across Ontario on the collective bargaining task force to share experience, strategy and information on settlements between the municipalities.

• Work in partnership with the City’s unions with the goal of keeping compensation increases at or below CPI.

• Continue to review performance and processes to become more efficient and cost-effective.

• Continue to obtain the best price for purchased services and supplies through the use of competitive tendering, forward contracting and purchasing consortiums.

• Continue to minimize the amount of goods purchased through conservation and reduction guidelines and policies.

• Maintain appropriate operating reserves for programs with expenditures that can vary significantly from year to year to smooth the budgetary impact.
Ensure City services respond to changing and growing needs:

- Use the City Corporate Planning process for priority setting to determine which services will be maintained or enhanced and which strategic capital initiatives will be undertaken.
- Include the costs of population and infrastructure growth in the budget.
- Require requests for operational service enhancements to include a business case identifying the additional revenue required and whether other services can be reduced or eliminated to pay for it.
- Take demographic changes into account when prioritizing and developing new City programs or services.
- Incorporate the equivalent of a 1% tax increase to go toward contributions to the strategic initiative category of the capital budget.
- Fund additional debt for growth-related projects from non-tax sources of revenue.
- Request that the Province change the development charge legislation so that all costs of growth are paid from development charges.

Explore new revenue sources:

- Increase current user fees by the percentage increase in the cost of providing the service to maintain the existing tax-to-user-fee ratio.
- Ensure that user fee increases do not reduce the number of people using those services.
- Move towards implementing new user fees for programs or services when specific users can be identified.
- Define a target tax-to-user-fee ratio for major service areas for Council approval.
- Request the Province to provide access to other forms of revenue.

Ensure infrastructure projects are adequately funded:

- Increase contributions to the capital budget at the rate of increase in the Infrastructure Construction Price Index, as set by Statistics Canada, to ensure the City’s contribution to capital is not eroded by inflation.
- Set infrastructure renewal as the priority for capital funding by increasing contributions to the capital budget.
- Continue to minimize the amount of debt used for infrastructure renewal and set the amount of tax-supported debt to a fixed percentage of the total tax bill.
• Maintain a minimum tax-supported reserve balance of $50 million to ensure emergency repairs can be managed.

• Work with the Province to identify new sources of revenue to fund capital renewal and rehabilitation in the new Municipal Act.

• Request that the Province both maintain and enhance current renewal subsidy programs.

• Given Ottawa’s uniquely rural and urban geography, work with the Province to ensure that Ottawa has access to rural infrastructure programs and other future rural programs.

• Investigate new technologies that reduce maintenance requirements or extend the life of a capital asset.

• Introduce programs that reduce consumption, thereby increasing the life of the existing assets and reducing the need to expand to accommodate growth, (e.g., increasing the modal split, smart meters for water consumption).

• Set the amount of tax-supported debt to a fixed percentage of total taxes.

Better deal with expenses incurred today but paid for in the future:

• Report tangible capital assets in the 2009 financial statements and increase contributions to the capital budget each year by the amount that new tangible capital assets add to the depreciation expense.

• Incorporate a landfill liability charge into the garbage fee.

• Defer the post-closure costs for landfills by extending the life of landfills through increased diversion rates.

• Develop a strategy to fund, over time, post-employment or retirement employee benefits liabilities.

LRFP III provides information the new Council will need when working with residents to develop a new Corporate Plan that will identify priority programs and services. This will lead the way to developing a multi-year budget that will allow the City to deliver on its priorities. This important debate will shape the City’s future over the next term-of-Council while moving towards long-term financial sustainability. The LRFP will be updated at the end of Council’s four-year term or earlier, if there are significant changes in the City’s financial situation.