

## ADMINISTRATIVE REPORT

Date: December 03, 2001  
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TO: Vancouver City Council

FROM: General Manager of Corporate Services / Director of Finance  
in consultation with the Corporate Management Team

SUBJECT: 2002 Operating Budget - Preliminary Report

### **RECOMMENDATION**

- A. THAT Council receive the preliminary report on the 2002 Operating Budget for information and instruct the Director of Finance to meet with departments and boards to review the underlying estimates with a view to ensuring that:**
- ▶ *the budget includes funding only for service and program levels approved by Council; and*
  - ▶ *all requests for additional or new services are removed from the estimates and referred to Council for approval.*
- B. THAT the Director of Finance, in consultation with the Corporate Management Team, report the interim estimates to Council in March, 2002 along with options to achieve a property tax increase that reflects inflationary levels.**
- C. THAT Council reiterate its policy that all requests from departments and boards for service level or program funding increases be accompanied by related offsetting revenue increases or expenditure reductions, such that**

*there be no net increase in Operating Budget funding requirements, and*

*THAT all requests requiring additional funding in the 2002 or 2003 Operating Budget be deferred for consideration as part of the interim budget report.*

- D. THAT Council instruct the City Manager to report back on the need and process for a public consultation initiative related to the service level and taxation choices required to balance the 2002 Operating Budget.*

### **COUNCIL POLICY**

*It has been Council policy that general purpose tax increases associated with development of the Operating Budget be held within the range of local inflation. However, in approving the annual budget, Council has adopted a practice of passing tax increases related to requisitions from outside agencies, including the Greater Vancouver Sewerage and Drainage District, through to taxpayers rather than forcing offsetting reductions in City programs and services to meet Council's taxation objectives.*

*It is Council policy that changes in service levels, either expansions or reductions be approved by Council. This includes the creation and deletion of regular positions and the allocation of funding from revenues or taxation.*

### **PURPOSE**

The purpose of this report is to advise Council of factors influencing growth in the 2002 Operating Budget and to seek Council input to the budget development process.

### **BACKGROUND**

The Vancouver Charter requires the Director of Finance to present the budget estimates of revenues and expenditures to Council not later than April 30 each year and for Council to adopt a resolution approving the budget and a rating bylaw establishing general purpose tax rates as soon thereafter as possible.

There are generally three reports to Council in the budget building process.

- the preliminary report provides Council with the first indication of the budget requests from Departments and Boards and seeks guidance on Council's taxation objectives and the policies that will govern the administrative review of the estimates.
- the Interim Report summarizes the results of the detailed administrative review of the budget and seeks Council approval to finalize the estimates, bringing the budget into balance. This report will follow the budget review process and is anticipated in early March, 2002.
- the Final Report on the Operating Budget presents the finalized revenue and expenditure estimates including any final adjustments approved by Council at the interim report stage. The Final Report is accompanied by a resolution in which Council adopts the estimates for the year. This report is anticipated to be before Council in early April, 2002.

### The Operating Budget

The City provides a wide variety of programs and services to people and property. The primary areas in which these services are grouped and the corresponding 2001 budget allocations are summarized in the Figure 1.

Utilities (Water, Solid Waste, Sewers)	\$136.5 million	21.4%
Other Public Works	44.1 million	6.9%
Public Safety	207.6 million	32.7%
Recreation and Community Services	124.8 million	19.7%
General Government	61.8 million	9.7%
Capital Program	55.3 million	8.7%
Transfers	<u>6.3 million</u>	0.9%
Total	\$636.5 million	

Of these expenditures, approximately \$105 million - the water and solid waste utility and a portion of the sewer utility - are funded from consumption-based user fees. The balance of the expenditures, approximately \$530 million, are funded from the annual operating budget.

In developing the annual budget, the cost of providing these services, along with any additions approved by Council, are adjusted to ensure that service levels are maintained from one year to the next. There are a number of factors that influence the cost of providing these services, including collective agreement provisions for City staff, inflation in program costs, the cost of new or expanded services approved by Council and the impact of the capital expenditure program.

The legislation governing the City requires Council to maintain a balanced budget. As

indicated in Figure 2, the City has limited access to sources of revenue to cover these expenditures. Within the authority provided by the Vancouver Charter, Council has employed a variety of revenues focussed primarily on fees and charges for specific services, transfer payments from the provincial government and miscellaneous income. However, almost two thirds of the revenue to offset the cost of services provided by the City comes from the property tax levy.

**Figure 2: Sources of Revenue**

Property Tax	\$ 372.2 million	58.6%
Other Taxation	40.1 million	6.3%
Utility Fees	103.9 million	16.3%
Licence & Inspection Fees	36.2 million	5.7%
Park Board Revenues	25.8 million	4.1%
Street Parking Program	23.9 million	3.8%
Short Term Interest	11.4 million	1.8%
Provincial Revenue Sharing	6.0 million	0.9%
Civic Theatres Revenues	5.3 million	0.8%
Transfers In	<u>10.5 million</u>	1.6%
Total	\$635.5 million	

Building the budget each year involves a process of offsetting program expenditures with general revenues and utilizing property tax increases as the balancing item. As Council has maintained a policy of holding the increase in property taxes at or near the level of inflation, important trade-offs are required between the types and levels of service to be provided and the extent to which additional cost can be added to the property tax levy.

## **DISCUSSION**

### **2002 Preliminary Estimates**

The preliminary report on the Operating Budget provides the first opportunity to review the factors influencing the changes anticipated in the 2002 expenditure program, the availability of additional general revenues to offset these costs, and the estimate of the general purposes property tax increase that would be necessary to maintain approved service levels.

Development of the 2002 estimates has involved a review of both revenue and expenditure budgets in the tax-supported programs. The projections do not deal with the user fee supported utility budgets that are being reported separately to Council. However, as these costs are also charged to the same properties that pay property taxes, their impact is factored into the discussion of overall City charges faced by taxpayers later in this report.

The preliminary estimates have not been subject to the detailed administrative review that

will take place during January and February. However, the estimates do present an overall picture of where staff expect the 2002 Operating Budget to be once that process is complete. As such, the estimates help to identify any gaps between the indicated tax increase and Council's taxation expectation that could necessitate adjustments on either the revenue or expenditure side of the budget.

The following table summarizes the current position of the 2002 Operating Budget and provides a comparison with the 2001 Operating Budget:

Figure 3	2001	2002	% Change
	(\$000)	(\$000)	
<b>Revenues</b>			
Taxation Revenue	\$412,288	\$414,905	0.6%
General Revenue	77,602	73,623	-5.1%
Transfers	<u>10,486</u>	<u>11,510</u>	9.8%
Total Revenues	\$500,376	\$500,038	-0.1%
<b>Expenditures</b>			
Departmental Expenditures	440,212	\$460,815	4.7%
Capital Program	55,322	59,912	8.3%
Transfers	<u>4,842</u>	<u>4,955</u>	2.3%
Total Expenditures	\$500,376	\$525,682	5.1%
<b>Shortfall</b>	<u>\$ 0</u>	<u>\$ 25,644</u>	
<b>Projected Tax Increase</b>		<u>6.8%</u>	

As can be seen by the table, the expenditure budget is expected to grow faster than the revenue budget, resulting in a shortfall of approximately \$25.6 million. Without further action, a property tax increase of 6.8% would be required to offset this shortfall.

The following sections summarize the major drivers in this budget position.

### The Expenditure Estimates

Overall, the expenditure budget is anticipated to increase by 5.1% to \$525.6 million.

a) Departmental Expenditures

More than 85% of the tax-supported expenditure budget covers the costs of departmental programs and services. The 2002 estimates include \$460.8 million to support public safety, public works, community services, recreation, civic grant programs and a number of internal support services. This represents an increase of \$20.6 million (4.7%) over the 2001 level. This increase represents both inflation in base program costs and the addition of funding for new programs and services approved by Council (“added basic”) or arising from the capital program.

Maintaining base program expenditure estimates to approved levels is the primary objective of the budget program. This involves adjusting the funding available to programs to reflect only inflationary increases arising from collective agreements and general inflation and the additional costs associated with approved increases in service levels. Where efficiencies in service delivery are identified, adjustments are also made to expenditure estimates. Significant adjustments reflected in the 2002 preliminary estimates are summarized as follows:

- approximately 50% of the expenditure budget provides funding for the salary and benefit costs for employees who deliver City services to the public. Collective agreements covering these employees call for increases of 3.0% effective April 1 (2.25% effective increase in 2002) for all non-uniform staff and 2.95% effective January 1 for uniform staff at Police and Fire. Salary and benefit increases will add approximately \$13 million to the budget and account for more almost two thirds of the increase in departmental expenditures.
- a 1.75% increase has been provided in departmental budgets to allow for inflationary increases in non-salary, program costs. In addition, specific adjustments have been made in expenditure areas experiencing unusual levels of increase or reduction. General inflation is expected to add in excess of \$1.0 million to the 2002 budget.
- a portion of sewer costs remain funded from property taxes. A review of the distribution of sewer costs undertaken as a part of the user fee setting process for 2002 has identified approximately \$2.0 million in tax-supported costs that should be shifted to user fees.
- Contingency Reserve has been set at \$4.0 million at this preliminary stage of developing the budget. This provision will be available to deal with issues that arise throughout the budget process and will be reviewed prior to finalizing the 2002 estimates.

“Added Basic” is the operating cost of new programs and services approved by Council. These costs arise from Council approval for new or expanded programs or projects in the Operating Budget or from the costs of operating and maintaining new facilities included in the Capital Plan. In cases where there is not a specific offsetting revenue or recovery, these new expenditures add costs to the Operating Budget. There are a number of new/increased program expenditures that must be accommodated within the 2002 budget, including:

- in April, 2001, Council approved the addition of 50 sworn officers to the Police Department. Approximately \$2.5 million of funding must be added to the budget in 2002 to fund this increased staff complement.
- the estimates include \$610,000 in additional funding for the Park Board to annualize added basic costs approved in 2001 and to fund new operating costs to be added in 2002.
- requisitions from E-Comm for emergency radio and dispatch costs are expected to increase by \$630,000 (5.7%) in 2002. Total E-Comm requisitions remain below those anticipated in 1997 when Council agreed to participate in this service.
- Council has approved the extension of funding for a number of planning related studies, including the Downtown Transportation Plan and the Community Visions program.
- Council extended and expanded the GrowBusters program into the fall of 2002. Although these costs will be offset by increased permit revenues reported with the revenue estimates, the expenditure program will increase by \$330,000.
- Approval of a pilot street program as part of the Downtown Eastside Rehabilitation projected will cost \$335,000 in 2002. These limited-time costs are funded from the City’s share of gaming revenues reflected in the revenue estimates.

Taken together, the added basic costs in the 2002 budget are approximately \$6.0 million and are equivalent to a tax increase in excess of 1.6%.

b) The Capital Program

The City’s capital expenditure program is funded through the annual operating budget in the form of debt charges (principle and interest payments) on the debentures that finance them or in the form of a “pay-as-you-go” contribution (Capital from Revenue) from the current budget. Both of these components will increase in 2002 to maintain capital expenditures at the levels anticipated in the 2000-2002 Capital Plan:

- The 2000 estimates make provision for a net increase in debt charges of \$2.6 million, reflecting the impact of debenture maturities and the costs associated with a debenture issues undertaken in 2001 and a further issue scheduled for 2002.
- the Capital Plan has also scheduled an increase in Capital from Revenue of \$2.3 million, including \$750,000 of funding deferred from 2000.

This increase of \$4.9 million represents a tax increase of 1.3%

### **The Revenue Estimates**

As noted above, Council has limited access to revenues to offset the expenditure program and must therefore rely heavily on the property tax levy to fund the services provided in the Operating Budget.

As noted in Figure 3, the preliminary estimates indicate that revenues will remain close to the 2001 levels of approximately \$500.0 million, even after consideration of additional tax revenues from new value on the assessment roll and increases in fees and charges approved by Council. The lack of growth in the revenue budget places additional pressure on the property tax levy to fund the expenditure program.

#### **a) General Revenues**

General revenues are anticipated to decline by approximately 5.1%, or \$4.0 million to \$73.6 million, although this reduction does not take into account the availability of up to \$3.2 million of revenue from gaming in the City. Council will be consider the utilization of gaming revenue later in the budget process to assist in meeting its taxation targets.

The following issues are reflected in the preliminary estimates:

- although the Provincial Government has made no announcement, the budget continues to anticipate the receipt of \$2.5 million in traffic fine revenue sharing that has been received since 1999. Elimination of this funding would require adjustments to the budget equivalent to a 0.9% tax increase. In the longer run, it is anticipated that this revenue will increase beyond current levels.
- the economic situation in Canada and the United States has led the central banks to significantly reduce short term interest rates over the past three months. These reductions will have an impact on the performance of the City's short term investment portfolio, resulting in an anticipated reduction of 25% in earnings in 2002 to \$8.5 million.



- On Street Parking Revenue has been increased by \$750,000 to reflect the increase in parking meter rates approved earlier by Council.
- Licence and Service and Inspection revenues are expected to increase as a result of fee increases approved by Council, however, there continues to be concern that the current economic downturn will hold these revenues closer to the 2000 levels.
- Miscellaneous Revenue has been increased to reflect additional payments expected from TransLink for maintenance of the Major Road Network. The approval of the TransLink budget by the regional authorities should result in additional recoveries of \$900,000 over the 2001 level. Additional funding will also be provided by TransLink to the Capital Budget.

b) Taxation Revenue

Taxation revenues are those derived from property taxation sources and include the general purpose tax levy, payments-in-lieu of taxes paid by properties not subject to property taxation as well as penalty and interest charges for outstanding and arrears taxes.

The estimates for 2002 set these revenues at \$414.9 million, up \$2.7 million or 0.6% from 2001.

- Although the 2002 Assessment Roll will not be produced until January, it is anticipated that the general purposes tax levy will be set at \$371.7 million prior to consideration of a tax increase. This reflects a minor downward adjustment as a result of assessment appeals processed during 2001.
- initial information from the BC Assessment Authority indicates that non-market adjustments to the assessment roll will result in additional tax revenue of approximately \$3.6 million in 2002. This estimate is down significantly from the 2001 level (\$5.0 million) and will be confirmed with production of the 2002 Assessment Roll in January.
- The provision for adjustments to the tax levy arising from assessment appeals has been set at \$2.0 million based on initial discussion with the BC Assessment Authority.
- revenues from payments-in-lieu of taxes and penalty and interest income continue at 2001 levels of \$41.6 million, pending confirmation of the inventory of grantable properties and assessed values.

c) Transfers from Reserves

The transfer from other funds and reserves remain at 2001 levels and include:

- the annual surplus on the City's sinking fund, which assists with debt charges on debenture debt, is not expected to increase over the 2001 levels of \$3.3 million.
- the annual dividend from the Property Endowment Fund is fixed at \$7.0 million.

**2. Moving the Budget Process Forward**

As noted, the preliminary estimates leave the budget in a shortfall position of \$25.6 million prior to a detailed administrative review. The following summarizes the significant drivers in the budget resulting in this position:

Taxation Revenues	\$(2.6) million	(0.7)%
Revenue	0.4 million	0.1%
Departmental Expenditures	20.8 million	5.6%
Sewer Costs	(2.0) million	(0.6)%
General Government	4.2 million	1.1%
Capital Program	<u>4.8 million</u>	<u>1.3%</u>
Total	\$25.6 million	6.8%

Eliminating this shortfall and bringing the budget into balance will require some combination of additional revenues, changes to expenditure programs and/or a property tax increase. If a property tax increase alone were used to balance the budget, that increase would have to be 6.8%.

It can be anticipated that a detailed administrative review of the estimates will improve this budget position. In addition, Council will have the option of bringing gaming revenue into the budget. It might be expected that these actions could reduce the indicated tax increase by up to 1.5%, to about 5.3%. Figure 4 indicates the impact that a tax increase of this level would have on sample residential and commercial properties in Vancouver:

**Figure 4: Impact of a 5.3% Tax Increase**

	<u>Property Value</u>	<u>2002 Taxes</u>	<u>Change from 2001</u>	<u>Utility Fee</u>	<u>Total Increase</u>
<b><u>Residential</u></b>					
\$0.15 per thousand of taxable value					
• condominium property	\$150,000	\$475	\$23	\$9	\$32
• single family property	\$378,000	\$1,196	\$58	\$9	\$67
• single family property	\$600,000	\$1,899	\$92	\$9	\$101

Utility fees increase by 1.6%

**Commercial**

\$0.46 per thousand of taxable value

• commercial property	\$100,000	\$1,566	\$50	na	\$50
• commercial property	\$500,000	\$7,830	\$250	na	\$250
• commercial property	\$2,000,000	\$31,320	\$1,093	na	\$1,093

Sewer and Water fees increase by 1% and 7% respectively

1. Before 2002 roll adjustments and averaging
2. The municipal tax levy represents approximately 50% of a residential tax bill and 55% of a

The next step in the process of building the 2002 Operating Budget is for Council to refer the preliminary estimates to the Director of Finance for detailed review. As part of this review, each department and board will meet with the corporate Budget Office to review requests to ensure that only approved funding levels are included in the estimates. The review will also identify opportunities in the budget to reduce funding levels without impacting on services and also challenges that might require additional funding. Recommendations A and B of this report facilitates this referral and the subsequent report back to Council.

There are a number of issues that remain outstanding and must be factored into the current budget position:

- a decline in economic activity coupled with international events of the past few months have raised concerns about possible impacts on the City's budget. As noted above, adjustments have been made to revenues that are directly impacted by the economy, including short term interest earnings and fees and charges. Budget review will involve more detailed reviews of these areas of direct impact and of the less obvious areas that might be impacted by an economic downturn to ensure they are appropriately reflected in the budget.

- the Provincial Government is currently completing a review of the services it provides (the Core Review). The City is exposed to changes in provincial funding in a variety of ways and provincial decisions could have direct and indirect impacts on the 2002 and future Operating Budgets. It is anticipated that announcements about changes in provincial services will be made in January and February, 2002. Staff will continue to monitor the areas in the Operating Budget that face potential pressures as a result of changes in provincial funding levels and will report these to Council prior to finalizing the Operating Budget.
- there are a number of initiatives that will be seeking additional funding in the 2002 and 2003 Operating Budgets. The most significant of these is a request from the Police Department for additional sworn and civilian staffing. If approved, this request will require additional funding of approximately \$4.0 million over the next two years, equivalent to a tax increase exceeding 1.0%. This request for 30 sworn staff is the second part of a larger request for 123 positions submitted to Council in 2001 with a total annual cost exceeding \$9.0 million.

The extent to which these issues will impact on the 2002 Operating Budget will become clearer over the next few months as the budget building exercise continues. However, it is apparent that, coupled with the current budget position, it may be desirable for the City to engage the public in a dialogue about the choices that may be required between service levels and tax increases in bringing the 2002 Operating Budget into balance. Recommendation D instructs the City Manager to report back on the need for and process of conducting this dialogue in time to provide input to the 2002 budget decisions.

Given the position of the budget, any requests for additional funding in 2002 will be difficult to accommodate without placing additional pressure on property taxes. Recommendation C reiterates Council's policy that any requests for new or additional program expenditures should have no net impact on the Operating Budget; that either matching additional revenues related to the funding request or reductions in expenditures should be identified as part of the request. Moreover, it is proposed that all such requests be deferred for consideration as part of the overall budget decision making process in March, 2002.

## CONCLUSION

The current position of the 2002 Operating Budget indicates that a 6.8% property tax increase would be required to balance the estimates, prior to a detailed administrative review. While budget review and the possible inclusion of gaming revenue in the estimates will likely improve this position, it is clear that there will be some difficult decisions to make if Council's policy of holding property tax increases is to be achieved.

The recommendations in this report are intended to focus the attention of staff on developing a budget for 2002 that meets Council's longer term taxation objectives by limiting funding to approved services, identifying options for improving the current budget position and deferring any decisions on new or expanded programs or services until the budget position is more certain.

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