# City of Ottawa

## LONG-RANGE FINANCIAL PLAN III 2006 (PART 1 AND PART 2):

## FINANCIAL PROFILE OF THE CITY OF OTTAWA


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# EXECUTIVE SUMMARY

## 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."[A]

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.

[A] 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."[B]

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.

[B] Slack, Enid and Bird, Richard M. "Cities in Canadian Federalism." Presentation. Conference on Fiscal Relations and Fiscal Conditions. Georgia State University, Atlanta. May 2006.

## 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."[C]

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.

## POTENTIAL STRATEGIES OUTLINED IN LRFP III

### 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.

[C] Standards and Poors, Public Finance Report Card: Municipalities. May 25, 2006.

- 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.

## NEXT STEPS

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.

# INTRODUCTION

*Experts agree structural funding issues impede financial sustainability*

*Successful cities are essential to the success of the modern Canadian economy*

As continual corporations, municipalities keep and manage community wealth, in the form of assets, for generations. They plan for population growth, asset maintenance, demographic changes, emergency preparedness and a host of other eventualities that affect residents' quality of life. As such, they need a longer-term focus than most companies or other organizations. Since amalgamation, Ottawa City Council has recognized the benefits of long-term planning and incorporated this approach into the decision-making process by creating the Long-Range Financial Plans (LRFP) I and II.

The first and second LRFPs focused exclusively on planning capital spending. This third edition of the City's Long-Range Financial Plan (LRFP III) is a comprehensive financial document, which also includes operating and capital expenditures and an overview of the City's assets and liabilities.

The first Long-Range Financial Plan, tabled in 2002, examined concerns regarding the financial sustainability of Canadian cities. It summarized findings of major studies on municipal funding, which emphasized the new importance of cities in the global economy, and examined funding differences between major Canadian, European and American cities. The United States government and national governments in Europe are making major investments in their cities and have made numerous funding tools available to municipalities. The Canadian federal and provincial governments' progress in these areas is well behind Europe and the United States.

Since 2002, a number of other studies have confirmed that serious concerns remain about the sustainability of the fiscal framework under which Canadian municipalities must operate. These studies note that, while the federal and provincial gas tax provides cities with some help in the area of public transit, very little real progress has been made since 2002.

The major conclusions reached by these studies are outlined below.

One of the major economic and cultural shifts that has occurred with the advent of globalization is the emergence of cities as key drivers of national economies. In short, "…cities matter… Indeed, in Canada, as in most other countries, as large cities go so, increasingly, goes the country."[1]

In Canada, the health of cities is of primary importance to the national economy. It is anticipated that:

> "as much as 80 per cent of economic and population growth will occur in only six broadly defined city regions: the Greater Toronto Area, Vancouver and the lower mainland, Montréal and its environs, Ottawa-Gatineau, and the Calgary and Edmonton regions."[2]

[1] Slack, Enid and Bird, Richard M. "Cities in Canadian Federalism." Presentation. Conference on Fiscal Relations and Fiscal Conditions. Georgia State University, Atlanta. May 2006.

[2] Slack, Enid, Bourne, Larry S. and Priston, Heath. "Large Cities Under Stress: Challenges and Opportunities." Report. External Advisory Committee on Cities and Communities. March 3, 2006.

While there is no single definition for what makes a successful city, there are commonly agreed upon elements. These include high quality social and quality of life services, first-rate cultural infrastructure, good quality municipal infrastructure, an attractive natural environment, a diverse economy and the ability to attract and retain talented people.

Currently, Canadian cities are internationally recognized as successful. They are highly desirable places to live and work. When compared to American cities, they provide good social and cultural infrastructure and services while offering higher levels of personal security and safety. In 2005, Mercer International rated Ottawa 20th in the world for quality of life, ahead of Montréal and Calgary and most American cities. For cost of living, Ottawa ranked 122nd out of 144, making it less expensive to live in than Toronto, Vancouver, Calgary and Montréal.

However, the continued success of Canadian cities is at risk. The most significant reasons can be summarized as follows:

- Federal and provincial governments are "in effect downloading some of their deficits to those at the bottom of the fiscal food chain – local governments."[3] This has been done in a number of ways: by directly offloading services to municipalities (e.g., provincial highways, ambulance service, social services and social housing); by reducing transfer payments to municipalities (e.g., provincial transfers for public transit); by reducing direct government expenditures in areas that directly impact local areas (e.g., reductions to immigrant services and funding for health supports for low income and disabled people); and by imposing "unfunded mandates", where regulations have increased municipalities' expenditure requirements (e.g., water quality standards).
- To remain competitive in the national and international marketplace, cities must provide state-of-the-art transportation and communications infrastructure, high quality cultural and recreation facilities and programming, and reliable emergency and police services.
- Cities experiencing rapid growth are also experiencing higher costs, due to the high costs of building new infrastructure and of maintaining infrastructure that is under stress from a growing population.
- Increased pressures on the expenditure side have not been balanced by corresponding increases on the revenue side. Canadian cities can only raise revenues through property taxes, user fees and development charges. Unlike sales and income taxes, property taxes do not grow with the economy.

[3] Slack, Enid and Bird, Richard M. "Cities in Canadian Federalism." Presentation. Conference on Fiscal Relations and Fiscal Conditions. Georgia State University, Atlanta. May 2006.

*There is a municipal fiscal imbalance that threatens Canada's prosperity*

All of the studies conclude that, while Canadian cities are providing most of the services that lead to economic growth, they do not have adequate financial tools to fund those services. Economic growth increases federal and provincial revenues far more than those of municipalities. This creates a fiscal imbalance for municipalities.

A fiscal imbalance exists when:

> "The fiscal capacity of one order of government is insufficient to sustain its spending responsibilities while the fiscal capacity of another order of government is greater than is needed to sustain its spending obligations, while both orders of government provide public services to the same taxpayer."[4]

Cities in Canada are creatures of their province. This means that cities do not have control over many of the services they provide and are restricted in their abilities to raise revenues. Cities are subject to the whims of the province in terms of services, service levels and funding. While the current debate in Canada is the federal/provincial fiscal imbalance, most experts agree that the municipal fiscal imbalance is at least as important if not more so.

An analysis of the relative expenditures and revenues of the federal, provincial and municipal governments from 1988-2004[5] reveals the following:

- While its revenues have been increasing, the federal government's expenditures, per capita, have been declining. Provincial/territorial government expenditures have been increasing at a lower rate than revenues. Municipal government expenditures have been increasing at a faster rate than their revenues.
- Provincial/territorial governments have seen the highest average annual growth rate in revenues.
- Federal and provincial tax revenues, per capita, increased over the 16-year period while municipal tax revenues remained fairly flat.
- Federal and provincial/territorial governments rely on personal and corporate income taxes and consumption taxes, along with other tax and non-tax revenues. Some provincial governments (including Ontario) also levy a property tax. Municipal governments rely mainly on one tax – the property tax.
- A greater increase in provincial property taxes for education and relatively smaller increases in municipal property taxes "suggest some crowding out of municipal tax room by the provincial property taxes…"[6]

[4] Kitchen, Harry M. and Slack, Enid. "Trends in Public Finance in Canada." May 24, 2006.
[5] Ibid.
[6] Ibid.

The studies all agree on two key points regarding the municipal fiscal imbalance:

- Municipalities do not have revenue-raising tools to allow them to adequately meet their responsibilities.
- Cities do not have sufficient control over their own destinies and are constrained from solving their own fiscal problems.

*The existing funding framework means Canadian cities are not able to adequately maintain infrastructure*

With more than 80% of Canada's population living in cities, and the vast majority of its businesses centred there, investments in high-quality infrastructure are vital to Canada's economic success. Specifically, the availability and quality of services provided by local infrastructure – water, sewers, solid waste facilities, public transit and transportation systems, cultural and recreational facilities – are critical factors in improving economic growth, productivity and international competitiveness.[7]

Ottawa's first Long-Range Financial Plan examined the importance of municipal infrastructure, and identified the significant differences between the large-scale investments made by Europe and the United States in municipal infrastructure as compared with Canada's investments.

There is agreement that there is a significant and growing infrastructure gap in Canada, and that it was largely created when federal and provincial infrastructure funding streams were replaced by ad-hoc infrastructure programming. American and European governments have recognized the critical role infrastructure plays as the backbone of every large city's economy; conversely, investment in infrastructure by Canada's federal and provincial governments has been declining. Canada remains the only G8 country without a national transportation infrastructure program. Moreover, given the limits to municipal funding tools, most municipalities have had little choice but to "systematically [under-invest] in infrastructure, both hard and soft infrastructure (e.g., transportation, roads, water, sewers, recreational facilities, community services, etc.)"[8] to balance their budgets and limit their debt.

Statistics Canada estimates the value of Canada's existing public infrastructure at $157 billion.[9] A number of recent studies have attempted to measure Canada's infrastructure gap, and estimates range from $60 billion to $125 billion, depending on the infrastructure included and the methodology used.[10] Even when the lowest estimate is used, the infrastructure gap is significant and the studies agree that it must be addressed if Canada is to remain internationally competitive. Given that municipalities in Ontario have responsibility for most of the province's physical infrastructure assets (62%, compared to 23% for the province and 15% for the federal government), this gap is a particular challenge for Ontario's two largest cities, Toronto and Ottawa.

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[7] Government of Canada. Fall 2002. Speech from the Throne.

[8] Slack, Enid, Bourne, Larry S. and Priston, Heath. "Large Cities Under Stress: Challenges and Opportunities." Report. External Advisory Committee on Cities and Communities. March 3, 2006.

[9] Research Analysis Division, Infrastructure Canada. "Productivity and Infrastructure: A Preliminary Review of the Literature." August 2006.

[10] The range varies because each study looks at different parts of the infrastructure and different data. Infrastructure Canada has very recently begun a comprehensive literature review in order to develop a workplan to address existing knowledge gaps about the specific nature of Canada's infrastructure gap.

The conclusion reached by the studies is clear, and can be best summarized by the following:

> "As municipalities grow and age, attention must be devoted to the expansion or replacement of their capital stock. Water plants and sewage treatment facilities must be enlarged or rehabilitated. Transportation and communications facilities must be updated and extended. Brownfield remediation must be addressed and 'blighted' areas of cities revitalized and redeveloped. The need for increased infrastructure funding in Canadian municipalities has been advocated by the Federation of Canadian Municipalities for some time and more recently, by the mayors of the large cities."[11]

Municipalities will not be financially sustainable without new funding tools and without authority over the services they provide.

## FOCUS OF LRFP III

The focus in this third LRFP is on improving the City's financial sustainability, including the strategies and policies that need to be implemented to achieve long-term stability. As directed by Council, LRFP III gives an overview of the factors that influence the City's financial situation and outlines strategies the City will need to consider to become financially sustainable in the long-term and provides a forecast of the operating pressures facing Ottawa over the next four years and the capital requirements over the next 10 years. It also provides options for City Council's consideration for the short- and medium-term. The LRFP offers a framework to help develop future budgets and frame discussion with other levels of government and the community.

This document will provide Councillors with the information they need when setting term-of-Council priorities. It will also guide the City's financial development over the next four-year term-of-Council. The document will be updated at the end of the four-year term or earlier, if there are significant changes in the City's financial situation.

### Defining financial sustainability

There are many definitions of financial sustainability, but for municipal government purposes, the definition used by the Local Government Association of Australia is the easiest to understand and the most comprehensive. The Association's definition of financial sustainability is:

> "…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."[12]

Using this definition, a municipality's long-term financial performance and position are sustainable when planned long-term service and infrastructure levels and standards are met without unplanned increases in rates or disruptive cuts to services.

[11] Kitchen, Harry M. "Physical Infrastructure and Financing." Research Paper. Panel on the Role of Government in Ontario. December 4, 2003.

A municipality would be considered financially sustainable if the following conditions were met:

- There is a reasonable degree of stability and predictability with respect to taxation;
- Future generations will not face massive decreases in services or unreasonable property tax rate increases to deal with items deferred from this generation;
- The current generation does not bear all the burden of funding items that will benefit future generations; and
- Council's highest priority programs (both capital and operating) can be maintained.

In the last two years, City staff have used a balance beam analogy when presenting the City budget to describe how yearly revenues must equal yearly expenditures. The balance beam analogy also applies to discussions about financial sustainability. To achieve a balanced budget, both sides of the balance beam require adjustment. Every year, some expenditures must be reduced or eliminated and new revenues found to accommodate changes to the individual components that comprise total expenditures and revenues.

The following graph shows the balance beam for a single budget year and includes these expenditure items:

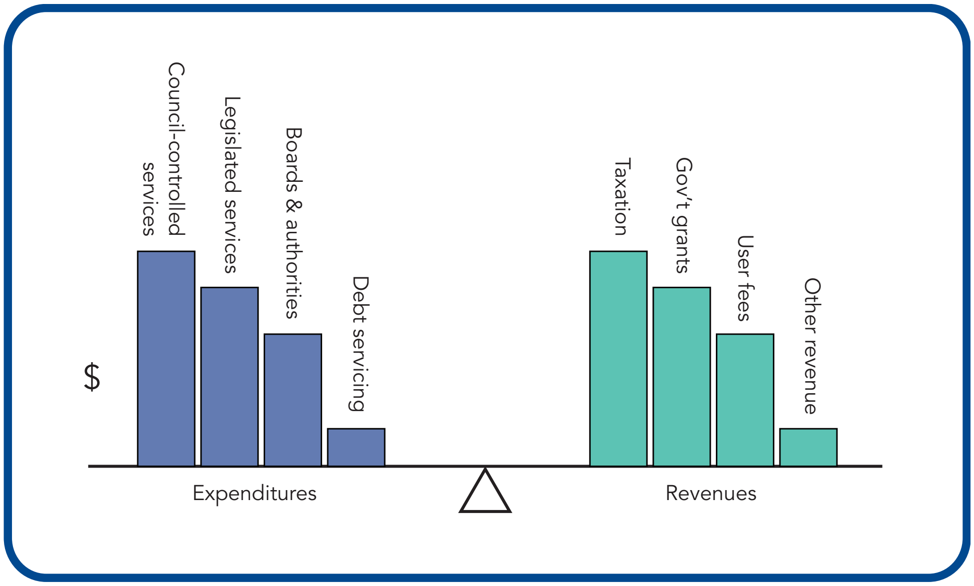
- Council-controlled services (e.g., fire, libraries, contributions to capital)
- Legislated services (e.g., employee and financial assistance, paramedics, housing)
- Boards and authorities (e.g., police services)
- Debt servicing (i.e., the fixed repayments required for previously issued debt)

The revenue items include:

- Taxation derived from property assessment
- Government grants and subsidies (conditional or unconditional)
- User fees (e.g., water consumption fees, recreation fees, transit fares)
- Other revenue (e.g., interest earnings)

[12] Local Government Association Financial Sustainability Program, Australia

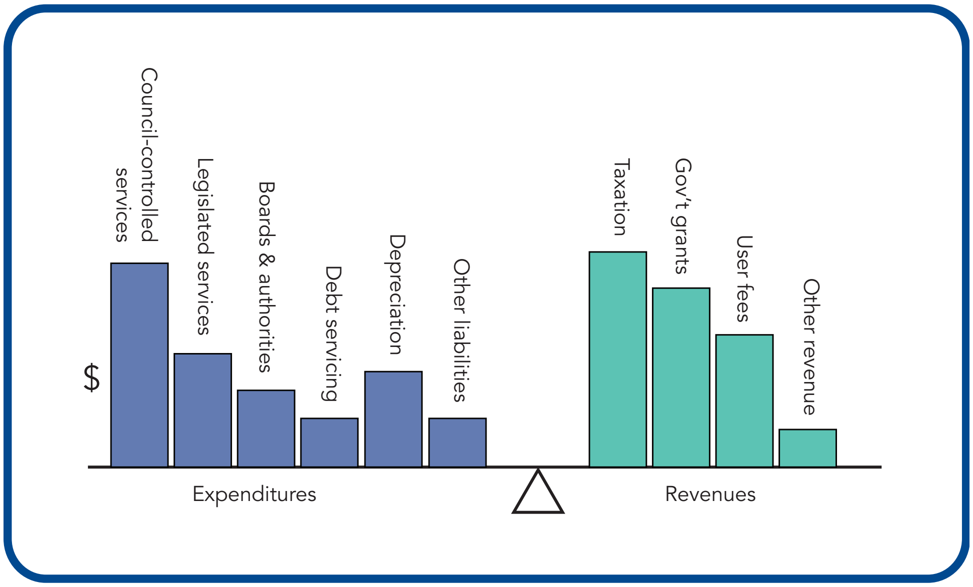
### Current year budget balance beam




As each component in the balance beam is subject to long-term fluctuations, organizations that are sustainable over the long-term try to smooth the adjustments required to remain in balance from year to year. One of the ways to accomplish this is to ensure that benefits received today are paid today and that expenditures are not deferred to future generations. This is referred to as inter-generational equity.

The following balance beam demonstrates how financial sustainability should look in a municipality. The expenditure side of the beam would list costs already found in the operating budget (Council-controlled services, legislated or mandated programs, boards and authorities, debt servicing). Longer-term liabilities (costs that will be incurred in the future from actions taken today) and the value of assets consumed during the period (depreciation) would also be added. To offset any increases on the expenditure side, either the existing sources of revenue are adjusted, other expenditures are eliminated, or new sources of revenue are identified.

## Municipal year budget balance beam




### How LRFP III fits into the City's integrated planning framework

When the first and second LRFPs were presented to Council, the City had not yet developed an overall, integrated planning framework. As a result, these documents became the strategic plans instead of the financial and funding strategies to support longer-term strategic business plans.

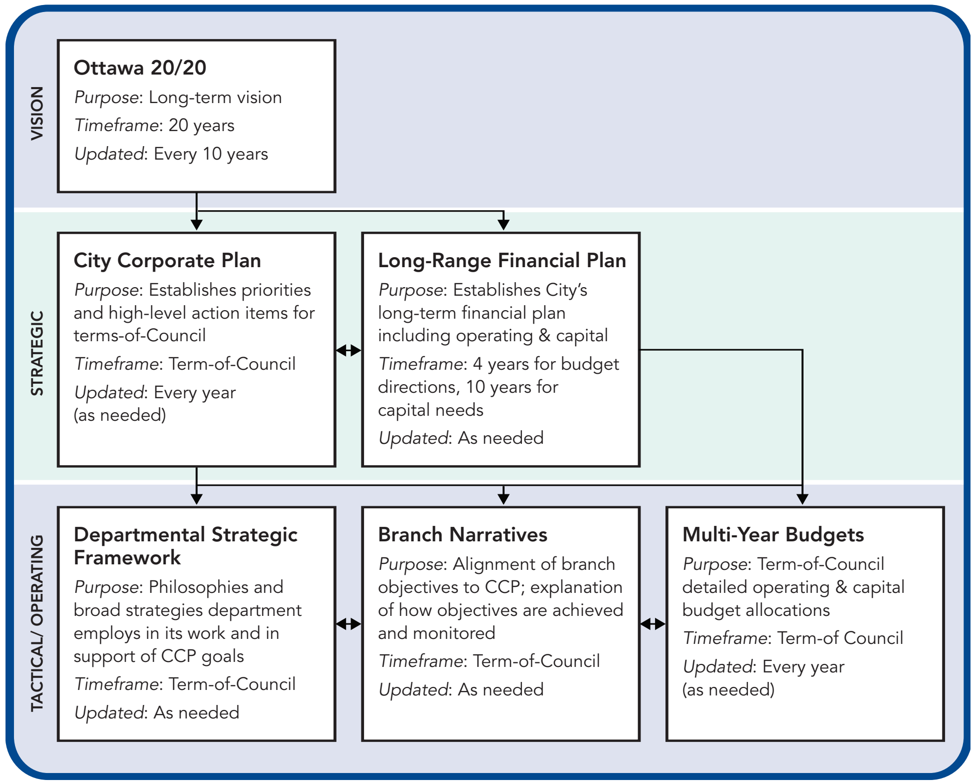
Council directed staff to prepare comprehensive planning documents, including a City Corporate Plan, to help set priorities for City spending.

The City Corporate Plan identifies Council priorities and establishes high-level actions and ongoing activities that the City will undertake to work towards delivering those priorities. Each action has a budgeted amount, which is included in the revenue forecasts provided in this LRFP.

The primary point of reference for the City's integrated planning processes is its strategic vision – Ottawa 20/20. Using the City Corporate Plan, Council establishes its priorities for how far and how fast it wants to move towards the Ottawa 20/20 vision. Those priorities must be established within a realistic financial context. Long-Range Financial Plan III outlines the City's financial condition and gives Council the financial context needed to set priorities.

LRFP III also outlines longer-term financial strategies that, if successful, would allow Council to advance its priorities and move towards financial sustainability. Term-of-Council budget directions will be developed to guide the formation of the budget each year. Additional detail on achieving Council's priorities is provided in documents such as departmental strategic frameworks and the operating branch narratives presented in the Budget. The actual 2007 Budget will not be provided for Council consideration until early 2007. The following graph shows the linkage between the various documents in the Integrated Planning Framework.

### Integrated planning framework




## Linkage with the annual budget process

As directed by Council, the City will provide operating and capital budget amounts for the upcoming year, early in 2007, that include a further three years of operating and nine years of capital forecasts. This will allow Council to see the longer-term impact of decisions made as part of the City Corporate Plan and LRFP approval process.

Actions approved in the City Corporate Plan are included in the operating and capital budget estimates, and the amounts included in those estimates are consistent with the forecasts provided in this LRFP. The forecasts for years two to four of the multi-year budget documents will be updated annually to account for any significant changes in assumptions and conditions. Each update will include a four-year budget forecast.

LRFP III outlines the options for Council consideration to continue providing a good quality of life for Ottawa residents while striving to keep property taxes at a reasonable level.

# ECONOMY AND DEMOGRAPHICS

Ottawa's robust economy centres on two major sectors – high technology and the federal government. Both sectors offer high-paying jobs for knowledge workers in a relatively stable environment and account for 37% of Ottawa's total gross domestic product (GDP). In 2004, the median family income in Ottawa-Gatineau was $73,500 – the highest among Canada's six largest cities.

**OTTAWA FAST FACTS**

- As Canada's capital city, Ottawa is a member of the G8 group of cities
- Fourth largest city in Canada by population
- Second largest city in Ontario by population
- At 2,796 sq. km, Ottawa is larger than the cities of Toronto, Montréal, Vancouver, Calgary and Edmonton combined
- More than $40 billion GDP
- More than $2.5 billion in venture capital investments since 2000
- One of the principal advanced technology centres in North America, with more than 70,000 high-tech jobs
- More than 25,000 employers
- More than 500,000 jobs

In 2001, the technology sector saw a downturn both in terms of employment and contribution to Ottawa's economy. Over the last year, however, advanced technology has shown signs of renewed growth. Overall, employment in Ottawa increased substantially in the first six months of 2006, and the local unemployment rate is at a low 4.8%, buoyed in part by a surge in non-residential construction.

The federal government has seen sustained growth since 2001. As a result, the Ottawa economy has continued to grow since then and employment has remained stable. However, government hiring has slowed since the election of a new federal government in 2006.

The City of Ottawa also benefits from a vital rural sector. In Ottawa, the rural economy contributes over $1 billion to the GDP. Agriculture alone accounts for $400 million, $136.7 million of which is farm-gate sales. Rural economic activity includes such things as agriculture, retail sales, construction, forestry and mining (aggregates), tourism, manufacturing, personal and business services, and transportation, to name a few. Rural employment expanded by a healthy 18% from 1996 to 2001.

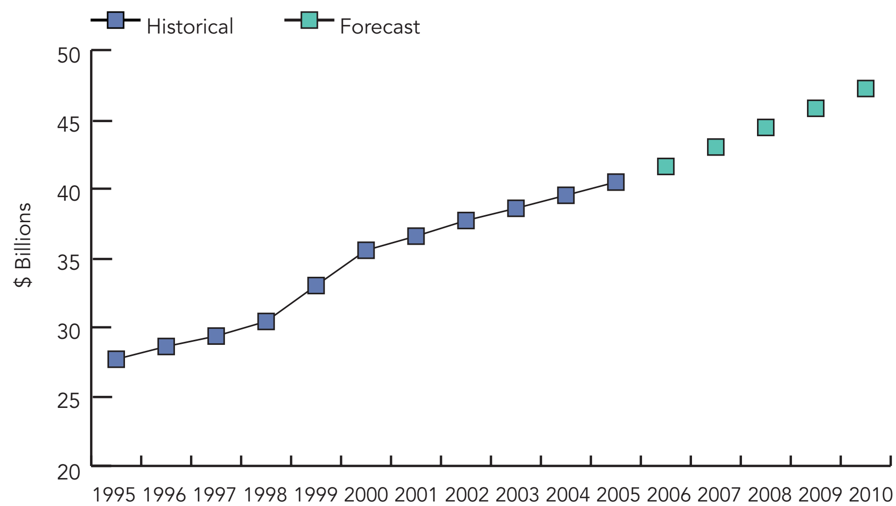
The Ottawa agricultural sector represents close to 300,000 acres of land farmed by more than 1,300 agricultural operations, employing approximately 10,000 people. Responsible, sustainable farming practices contribute to maintaining the value of Ottawa's countryside. Agriculture not only complements and affects the prosperity of other sectors such as rural tourism, but it also helps preserve the quality of rural Ottawa as a place to live and work.

Ottawa's GDP growth remained stable at 2.4% in 2005. The Conference Board of Canada's February 2006 forecast predicts that Ottawa's GDP growth will increase to 2.8% in 2006 and average 3.2% annual growth over the coming four years.

*Gross domestic product is steadily increasing*

Over the 2007 to 2010 timeframe, the Conference Board forecasts that Ottawa's GDP growth will be the seventh highest among the 20 largest cities in Canada, a significant improvement from its 13th place ranking in 2005. The following graph shows Ottawa-Gatineau's GDP from 1995 to 2010.

## GDP, Ottawa-Gatineau CMA




Source: Conference Board of Canada, Metropolitan Outlook, Feb. 2006

In its forecast, the Conference Board also examined the diversity of the city's economic base. As previously stated, the technology and federal government sectors account for 37% of total Ottawa GDP (see table below). This level of concentration means Ottawa relies heavily on these two sectors as the main drivers of its economy. Ottawa does not experience the same level of economic fluctuations seen in other municipalities because the federal government sector has been remarkably stable over the years and government employment does not tend to vary with economic cycles.

It is important to note that the reliability of the Conference Board's forecast hinges on growth in at least one of these two key sectors.

| Ottawa GDP by sector | |
|---|---|
| **Industry sector** | **% of total GDP** |
| High tech | 18.9% |
| Federal government | 18.2% |
| Tourism | 2.1% |
| Health and education | 7.5% |
| Finance, insurance, real estate | 10.4% |
| Trade | 9.4% |
| Construction | 4.0% |
| Primary (mainly rural output) | 0.9% |
| Others | 28.6% |
| **Total** | **100.0%** |

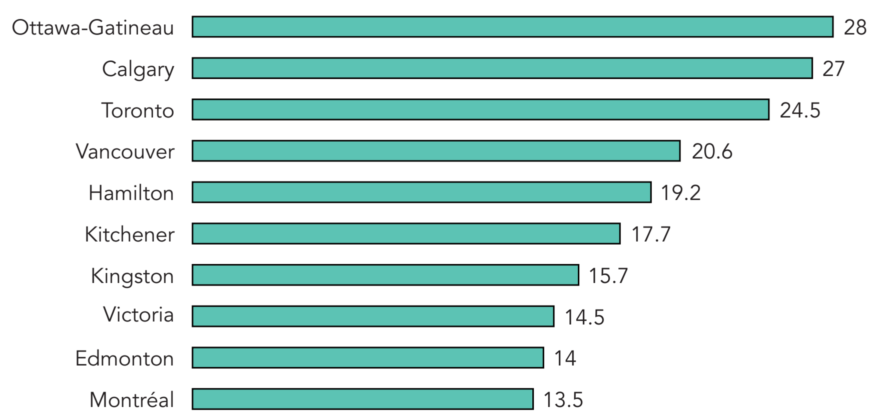
Source: Conference Board of Canada, Metropolitan Outlook.

CIBC's *Metro Monitor* reports on the rate of change in the level of economic activity among Canada's largest metro areas. The June 2006 index, which covers the first quarter of 2006, showed that the Ottawa-Gatineau economy registered the highest reading among all metro areas. The *Metro Monitor* notes that this ranking reflects a relatively diverse performance with the city's labour market clearly outperforming the national average from both quantity and quality perspectives.

In the first quarter of 2006, the Ottawa-Gatineau economy performed consistently well above average in most of the important indicators such as government, building construction, employment, and lower rates of business and consumer bankruptcies. The *Metro Monitor* also noted that the surge in high-tech activity is probably playing an important role in the city's impressive showing. There is a slight drag, however, on overall economic performance due to a slowing of the housing market.

### Top 10 metro economies* (2006Q1)

**3Q moving average**




Source: CIBC Metro Monitor

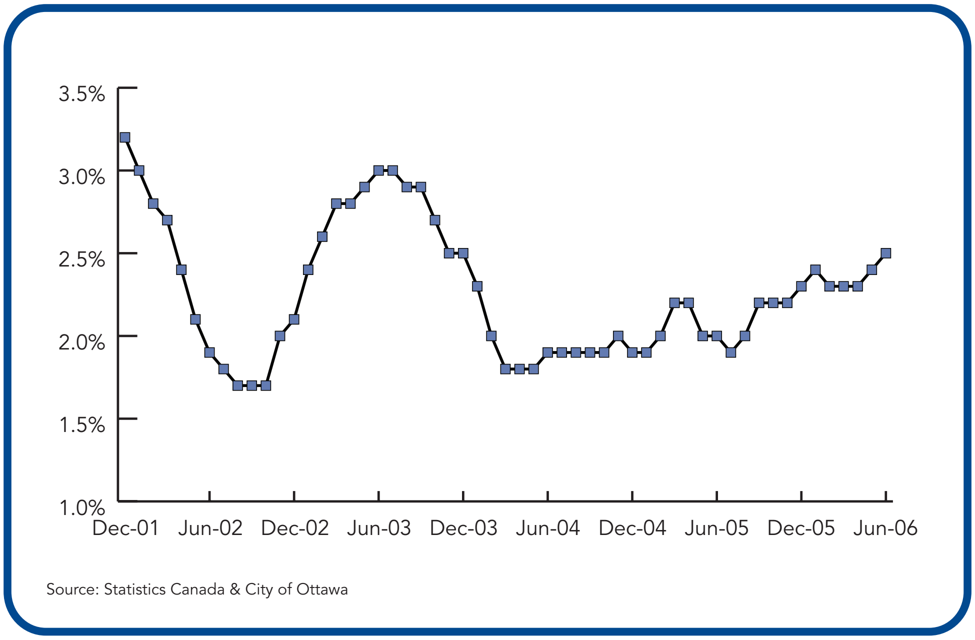
* CIBCWM Metropolitan Economic Activity Index

## *Inflation rates are low*

Annual inflation rates, as measured by the Consumer Price Index, averaged 2% from 2000 to 2004, exceeding 3% once in 2002. The CPI reflects the basket of goods consumed by a typical household. Low rates of inflation reflect the monetary policy the Bank of Canada favours to keep inflation within a range of 1% to 3%. Conference Board forecasts for Ottawa predict long-term inflation will average just over 2%. The following graph shows the inflation rate by month calculated as the average of the preceding 12-month period.

## Ottawa annual inflation

### 12-month moving average

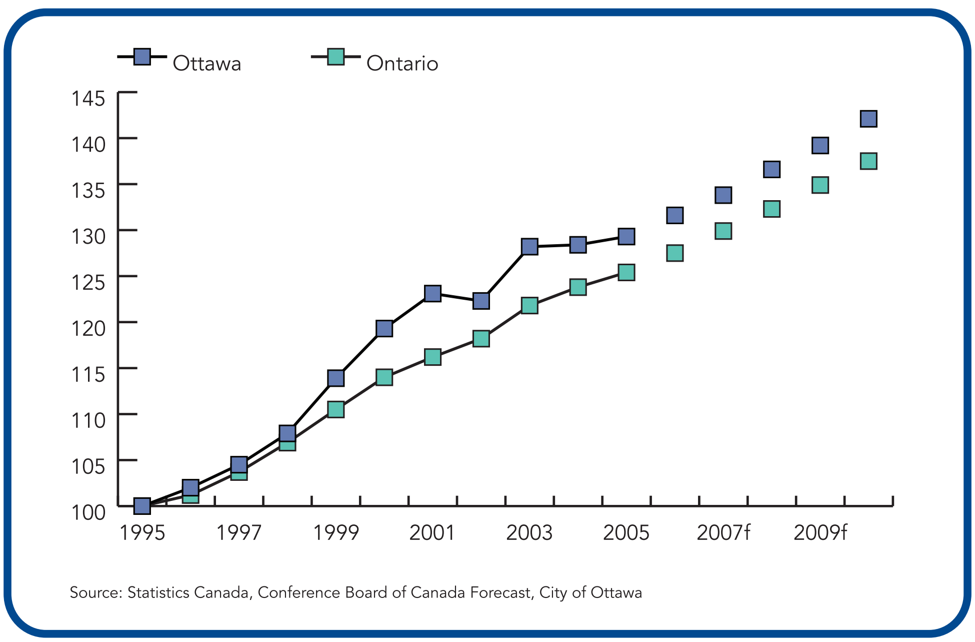



## EMPLOYMENT

*Employment is growing*

Ottawa experienced vigorous employment growth in the latter part of the 1990s and has posted employment growth comparable to the Ontario average since 2001. Employment levels in Ottawa, when measured as an index, have consistently outperformed the provincial average since 1999.

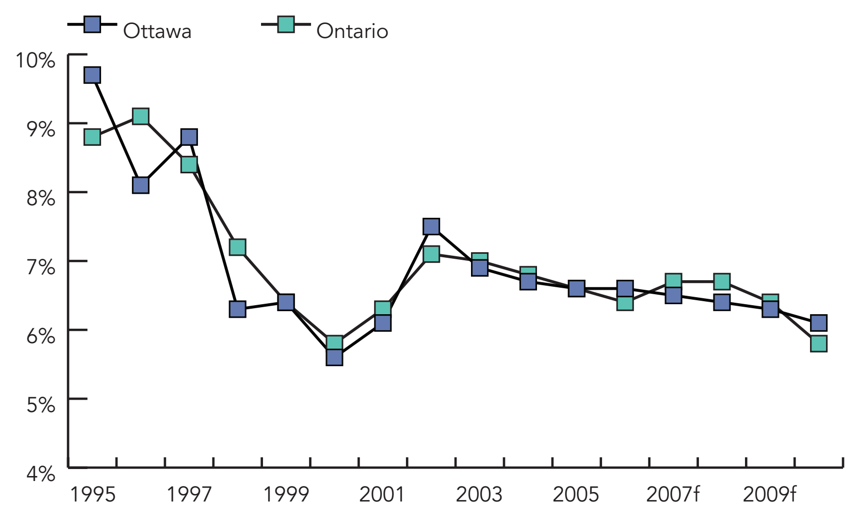
### Employment index, Ottawa and Ontario, 1995-2010



*Unemployment rate is stable*

Since the turn of the century, Ottawa's unemployment rate has been relatively similar to Ontario's. In fact, Ottawa's unemployment rate rarely surpassed the provincial average. Moreover, in the early 1990s, Ottawa had a significantly lower unemployment rate than the rest of Ontario. In 2002, however, the slow-down in the technology sector led to Ottawa experiencing a higher unemployment rate (7.5%) than the provincial average of 7.1%.

**Unemployment rate, Ottawa and Ontario, 1995-2010**




Source: Statistics Canada & Conference Board Forecast

## REAL ESTATE

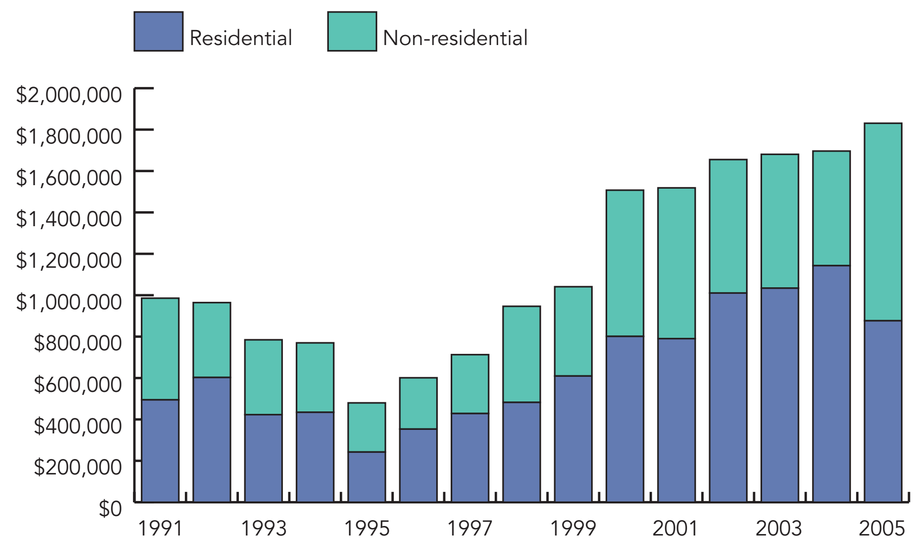
One of the measures of a city's economic success is the dollar value for building permits issued – it indicates how much growth is occurring in the city. Building permit value in Ottawa reached an all-time record of $1.83 billion in 2005, 7.9% higher than in 2004. At the national level, Ottawa-Gatineau ranks sixth among the major Canadian cities in terms of dollar value for building permits.

*Building permit value is increasing*

In 2005, the total building permit value for the Ottawa-Gatineau census metropolitan area (CMA) was $2.24 billion, a slight decrease of 1% compared with the previous year. This was mainly due to less industrial and institutional development in Gatineau, which translated to lower metropolitan growth averages. To date, 2006 building permit values for the Ottawa-Gatineau CMA are slightly ahead of last year.

The graph below shows the building permit values for the City of Ottawa from 1991 to 2005.

### Building permits, Ottawa, 1991-2005



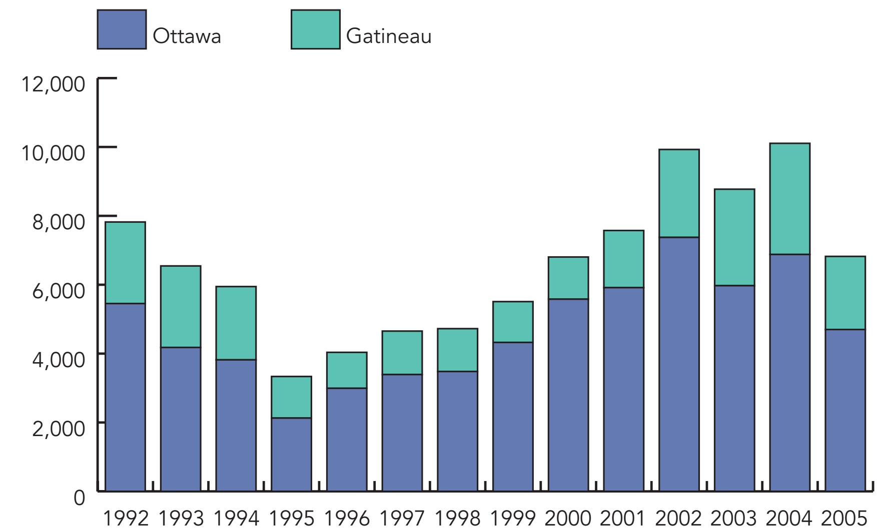

Source: Statistics Canada

Non-residential construction in Ottawa was responsible for the surge in activity in 2005. In fact, institutional and government construction projects more than tripled, fuelled by projects such as the Canadian War Museum, the new wing of the Royal Ottawa Hospital, major expansions at hospitals and universities, and ongoing renovation at several government buildings. Industrial construction increased by 110% over 2004, while commercial construction dipped by 8.3% and residential activity declined by 23.3%.

*Housing starts and rental vacancy rates are declining*

Low interest rates, a traditionally tight rental market, strong employment gains and steady population growth have fuelled Ottawa's real estate market over the past several years. Housing starts in Ottawa reached a cyclical peak in 2004, slowed down in 2005, but are 6% ahead of last year's levels as of the end of June.

### Ottawa-Gatineau housing starts, 1992-2005




Source: CMHC

In 2004, Ottawa residential Multi-Listing Sales ( MLS) reached a record high of 13,457 homes sold. In 2005, MLS sales dropped by 1.2% to 13,300 homes sold. However, combined Ottawa-Gatineau metropolitan MLS sales totalled 18,033 in 2005, making this the sixth most active MLS market in Canada. In 2005, the average price of a resale house in Ottawa was $248,358, up just over 4% from 2004.

After four consecutive annual increases, Ottawa's rental vacancy rate decreased to 3.3% in 2005, from a cyclical high of 3.9% in 2004. The decline is attributed to rising home-ownership costs, low rental construction, lower rents in many of the survey zones and, to a lesser degree, strong levels of youth employment leading to quicker departures from parental homes.

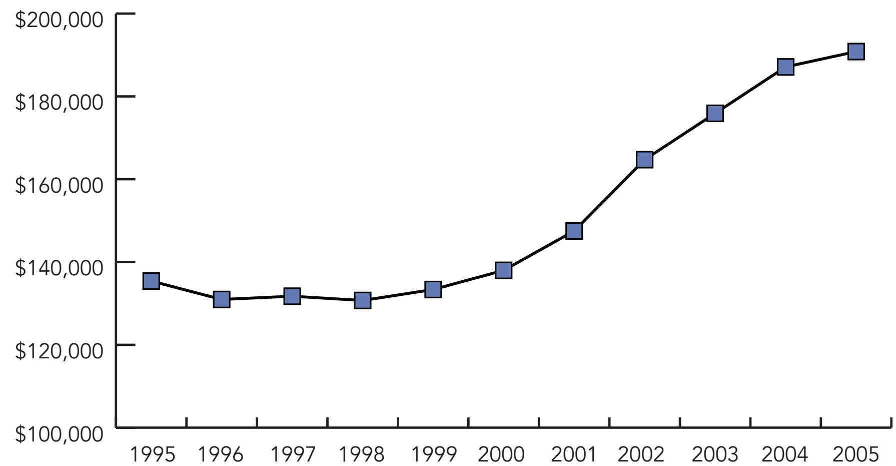
*Housing affordability is improving*

Home ownership has become slightly more affordable since 2005. In 2005, including both new and resale units, there were 4,428 affordable homes on the market (27.5% of the overall supply of housing). This is a small improvement over 2004 when 26.8% of homes were affordable.

However, as the following graph demonstrates, ownership prices have gone up in recent years, both for resale housing and new homes. In 2005, 5,466 houses were built in the City of Ottawa. Of these, 13.4% were affordable to households earning up to $56,800 a year, the 40th income percentile. Generally, affordability improved slightly in 2005 mainly because many new town homes were built.

In the residential resale market, 34.7% of homes sold were priced below $208,000 and were affordable to households at the 40th income percentile.

## Ottawa house prices adjusted for inflation




Source: Canadian Real Estate Association & City of Ottawa

Relatively low mortgage interest rates have meant that many householders could afford to own their own homes. The slight surge in the condominium market in recent years has also created more affordable ownership options. However, in 2005, the principal and interest charged on Ottawa's average condominium exceeded two-bedroom apartment rents, suggesting that condominiums are becoming a less affordable option to Ottawa residents. The average rent for a two-bedroom unit was $920 in 2005.

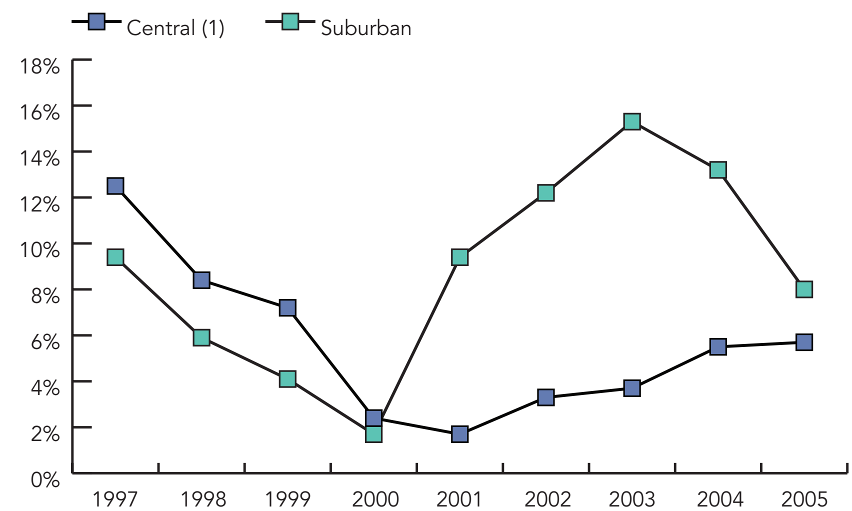
Housing affordability for tenants remains a problem in the city, where 35% of renters spend more than 30% of their income on housing. The affordable monthly rent for households up to the 30th income percentile in 2005 was $1,108. Fortunately, the picture is improving. Overall, average rents decreased for all types of apartments, except bachelors, in 2005. That same year, the number of renter households with affordability problems decreased a modest 12% from 1996 when 50,000 households paid more than 30% of their income for shelter.

*Office vacancy rates are stabilizing*

As the following graph demonstrates, Ottawa's market for office space in the central part of the city remained strong due to continued demand, primarily by the federal government. The suburban office rental market has declined since it peaked in 2000. The recent improvement in the technology sector has led to increasing demand for office space and a decline in suburban vacancy rates. By the end of 2005, overall vacancy rates declined 36% as more office space was used in the suburban market.

### Ottawa office space vacancy rates

**City central vs. suburban area**




(1) Central Area is Central Business District & Centretown but not Byward Market

Source: Cushman Wakefield LePage & City of Ottawa Tabulations

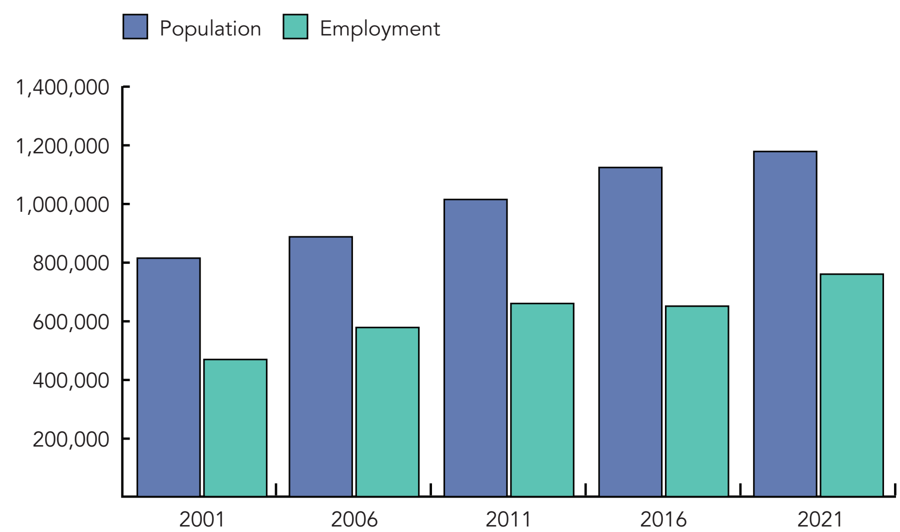
## POPULATION

Ottawa boasts a population of 870,250, which represents an increase of 7.9% since 2001. This growth rate is faster than Ontario's rate (6.2%) and Canada's rate as a whole (4.8%). Ottawa accounts for approximately two-thirds of the population of the greater Ottawa-Gatineau area, which has a combined total population of 1,282,500.

*The population is growing*

The population growth is expected to continue. The City's 2003 Official Plan predicted growth of 37% over the next 15 years. Recent growth trends have been somewhat slower than originally predicted, and this estimate may be revised in 2007. Even with the revision, it is clear that actual growth rates remain above average. Immigration is a major reason Ottawa's population continues to grow faster than that of Ontario or Canada.

**Projected population and employment growth, Ottawa, 2001-2021**




Source: Official Plan Projections

*The population is aging*

While Ottawa residents are slightly younger than the provincial average (11.5% aged 65 and over in Ottawa versus 12.9% aged 65 and over for the province), a significant demographic shift is occurring in Ottawa as the population ages, which is also part of a national demographic change.

The proportion of children in Ottawa has been dropping since the 1960s. Children below the age of 19 made up 40% of the city's population in 1966. Today, that age group represents approximately 25% of the population. Their share will drop even more to approximately 20% of the total population in 2021. In fact, every age group below age 55 will see a decline in its share of the overall population by 2021.

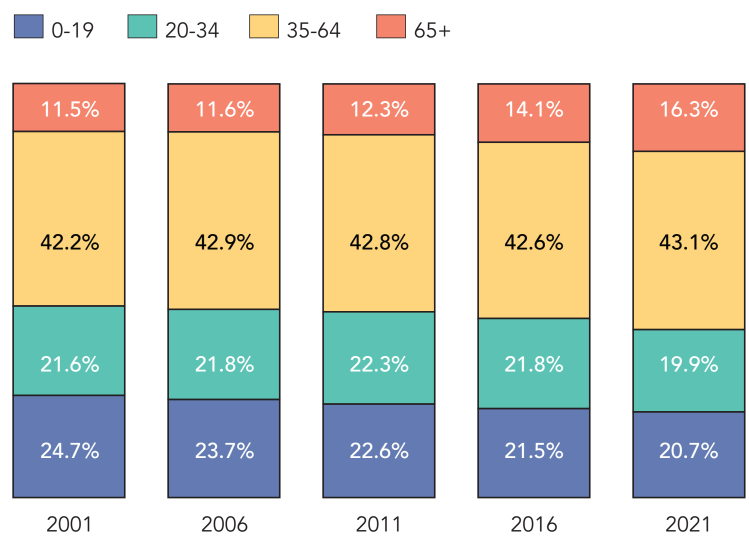
While the proportion of young adults (aged 20-34) was as high as 29% in the mid-1980s, it is now approximately 22%. This age group will increase its share of Ottawa's population between 2001 and 2016, reflecting the passage into adulthood of baby-boomers' children (baby-boom echo). By 2021, young adults will account for less than 20% of city residents.

Mature adults (aged 35-64) made up approximately 32% of the population in the mid-1960s. They now account for 41%, and their share will rise to 43% by 2021.

Seniors (aged 65 and over) represented approximately 7% of Ottawa's population in the 1960s. Their share has steadily risen to reach 11.5% as of the 2001 Census, and is predicted to represent just over 16% of Ottawa's population in 2021.

Changes in demographics influence the mix of City services provided to Ottawa residents.

## Projected population by age group, Ottawa, 2001-2021




Source: Official Plan Projections

Ottawa is becoming a significant point of entry into Canada for immigrants from around the world. Statistics Canada data show that immigrants to Canada tend to settle mainly in big cities. Immigrants who settle in Ottawa are attracted by high-paying professional jobs or post-secondary studies. They are typically more educated, earn higher wages, and have higher levels of employment than immigrants who settle in other cities. Ottawa also receives the highest percentage of refugees and family-related immigration of any major Canadian centre.

*Immigration is growing*

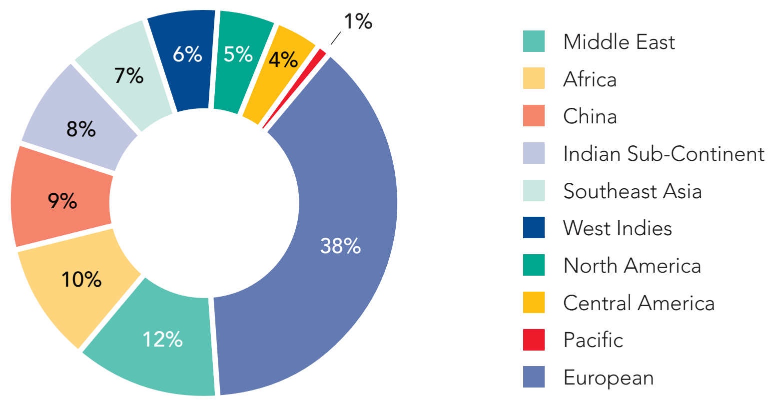
Between 1996 and 2001, Ottawa welcomed almost 25,000 immigrants from around the world. Recent immigrants – those who settled here in the past 10 years – make up 6.8% of the population, up from 4.2% in 1981. There are 70,500 recent immigrants now living here, representing the fourth highest concentration in the country.

Overall, 185,000 people born outside Canada reside in Ottawa. They make up almost 18% of our metropolitan population. While Toronto and Vancouver receive the most immigrants among the nation's big cities, Ottawa's immigrant population had the third highest growth rate (14.7%) between 1996 and 2001, tied with Toronto and trailing Vancouver (16.5%) and Calgary (15.5%).

### IMMIGRATION TRENDS 1996-2001

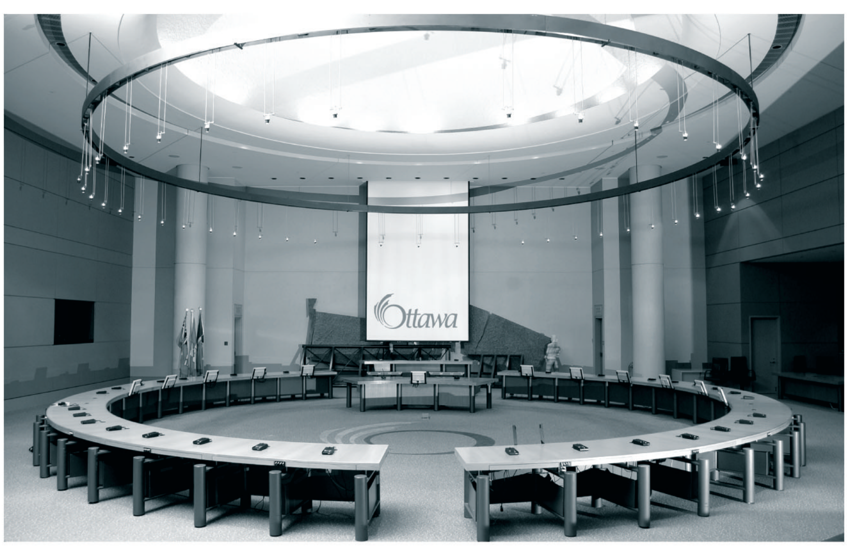
- Ottawa has Canada's third-largest **West Indian** community, and the second-fastest growing after Toronto. As of 2001, there were 11,000 people of West Indian origin living here.
- We have Canada's fourth-largest **African** community, and the second-fastest growing after Calgary. As of 2001, there were 19,000 people of African origin living here.
- Our **Chinese** community is the smallest of Canada's five largest centres (17,500 people), but it was the country's fastest-growing (65%) between 1996 and 2001.
- Our **Middle Eastern** community is Canada's fourth-largest, with 22,000 people.
- Our **European** community is the smallest of Canada's five largest cities, but it grew by 2% between 1996 and 2001. Calgary had the only other growing European community among the top five cities. In Toronto, Montréal and Vancouver, the European-born population shrank over the same five years.

### Total Ottawa-Gatineau immigrants, by place of birth, 2001




Source: Statistics Canada

# CITY OF OTTAWA FINANCIAL PROFILE




*The City has a very good credit rating*

Cities typically fund some of their capital costs by issuing debt – in the form of bonds – in the debt markets. Investors interested in purchasing this debt want to compare the bond's return to its risk. As a result, international rating agencies rate municipalities issuing debt to help investors determine the level of risk they would take if they purchased the bond. A high credit rating not only lowers the price of the bond, it makes the debt available to a wide range of Canadian and international investors. On the other hand, if a municipality's credit rating falls, it can increase the City's cost of borrowing and limit investors.

At this time, the City of Ottawa is rated by two international rating agencies: Moody's Canada Inc. and Standard & Poor's. Moody's recently confirmed an Aaa rating for the City – the highest possible ranking and one the City has maintained since 1975. In making its most recent assessment, Moody's notes that the City has performed well financially over the past several years, showing strict fiscal discipline and a commitment to long-range financial planning. Moody's also notes in this year's reporting, that the

> "…current plan (LRFP II) aims to phase out new debt issuance for lifecycle projects and restrict debt financing to expansion related projects or projects funded by development charges, third party funding or rate changes…. The City's adherence to a long-term capital plan, which ensures that debt levels and debt servicing costs remain modest, constitute a credit positive."

Standard & Poor's (S&P) has assigned an AA+ Stable rating to the City, taking into account the City's exceptionally stable economy, its current low debt level and continued high liquidity. Just one level below its highest, S&P defines this rating as:

> "An obligation rated "AA" differs from the highest-rated obligations only to a small degree. The obligor's capacity to meet its financial commitment on the obligation is very strong."

S&P expects that Ottawa's economy will retain its exceptional long-term stability and that increases in debt will be more or less contained to current forecast levels. In its analysis, the rating agency compares Ottawa to a peer group that includes Madrid, Oslo, Paris and Stockholm, and notes that Ottawa's debt level is very similar to that of Oslo and Stockholm, while its liquidity is the highest of this peer group.[13]

[13] Standard & Poor's rating report published June 30, 2005.

The City of Ottawa is an economic generator of significant importance locally and for Eastern Ontario and Western Quebec. Estimates show that City operations injected a little less than $1 billion directly into the Ottawa economy in 2004.

*The City is an important economic generator*

With approximately 17,000 employees on its annual payroll and a significant procurement and purchasing portfolio, the City of Ottawa makes a major economic impact. For example, City purchasing supports more than 7,000 vendors across the region, including approximately 1,000 rural suppliers. Purchased goods and services include: professional services, construction and technical services, general goods, and products and companies related to the maintenance of the City's fleet of equipment and assets.

This economic activity also supports employment, creates personal household income and generates revenue for the provincial and federal governments. Estimates of City-related local business volumes from secondary spending exceed $1.5 billion.

## PART A: OPERATING EXPENDITURES

In 2001, the amalgamated City of Ottawa was created to provide streamlined governance to residents and more efficient, cost-effective delivery of municipal services.

*Savings since amalgamation*

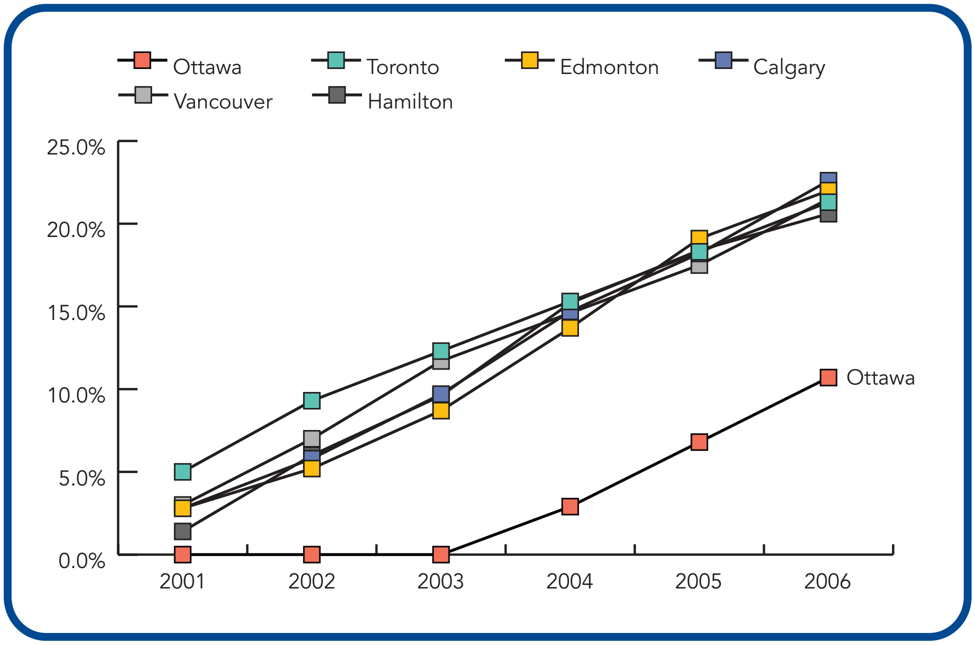
From 2001 to 2004, the amalgamation achieved over $101 million in permanent savings from: Opportunity Log items (i.e., items identified by City staff to be potential savings generators, such as business process improvements, organizational change, administrative efficiencies, technological enhancements and new revenues); internal service and discretionary budget reductions arising from the information in the Universal Program Review; and new ideas resulting from the Continuous Improvement Strategy adopted by City Council as part of the Opportunity Log.

These savings were significant – the equivalent of the combined municipal taxes collected by the former municipalities of Gloucester, Kanata, Nepean, Rockliffe, Vanier, Cumberland, Goulbourn, Osgoode, Rideau and West Carleton at the time of amalgamation. The City was able to achieve tax savings by focusing on finding major efficiencies without affecting service levels. Since the savings occurred in the three years after amalgamation, City Council was able to maintain existing property tax levels, while other municipalities across Ontario and the rest of Canada saw their taxes increase.

The following graph shows the cumulative per cent tax increase for a number of cities in Canada from 2001 to 2006.

### Property tax increases

**Cumulative yearly increase, by percentage**




Council and City staff saw the Amalgamation Savings Program as the beginning of a new City commitment to deliver services as efficiently as possible. Over the past five years, the City has embraced a culture of continuous improvement and developed leading-edge tools to help it improve its long-term financial sustainability; achieve annual savings from service delivery improvements, efficiencies and innovation; maximize the productivity of existing resources; and plan for future needs. These tools include:

- The City's first LRFP
- Universal Program Review (UPR)
- The Opportunity Log
- The Accountability Framework
- LRFP II
- Implementation of a performance measurement framework

The City has also piloted a Branch Process Review Program to examine its existing business processes. The program looks at identifying potential cost savings and financial management opportunities to realize efficiency potential within day-to-day operations.

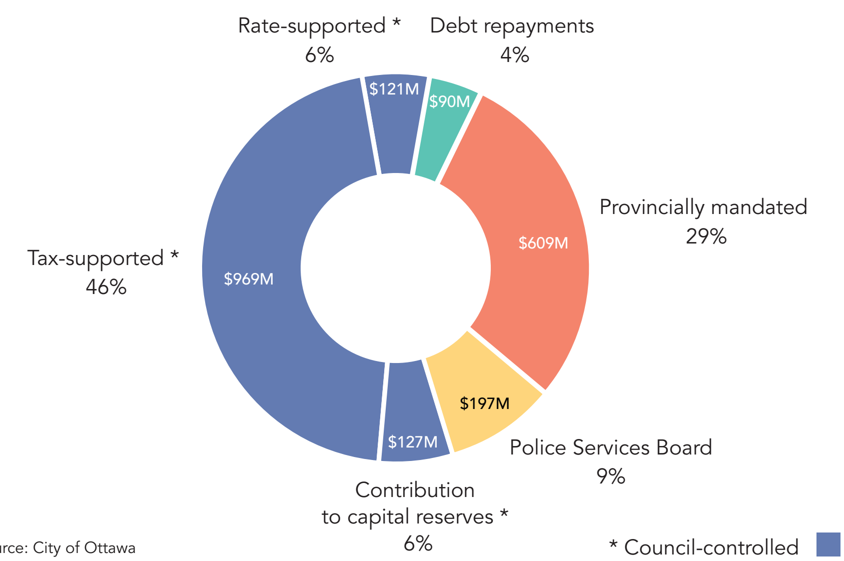
## EXPENDITURE OVERVIEW

Ontario municipal budgets include numerous programs and services that are provincially mandated but paid for through property taxes. As a result, there are many required expenditures over which Council has very little control. Ottawa's 2006 annual operating budget for tax-supported programs and services can be divided into the following categories:

- Provincially mandated or cost-shared programs
- Police Services Board
- Debt repayments
- Council-controlled expenditures

### Breakdown of operating expenditures

**2006 gross operating budget ($2,113M)**




Source: City of Ottawa

### Provincially mandated or cost-shared programs

The Province has established programs for a variety of services such as social assistance, social housing, child-care, public health and many others. When these programs were set up, the province set the regulations, established the cost-sharing formula, and then required the City to administer these programs on its behalf. Almost one-third of City spending is directed to provincial programs.

Over the years, the level of provincial funding based on cost-sharing formulas has deteriorated. Expenditures that were originally eligible for cost-sharing are now deemed ineligible. As service costs grow, funding caps cover a smaller proportion of these expenditures and municipal property tax funds have to make up the shortfall.

### Police Services Board

Comprising Councillors and appointed members of the public, the Police Services Board oversees the police department and makes independent decisions about the priorities and needs presented to Council. The Police Services budget represents 9% of gross City spending. Council can either reject or approve the budget in its entirety, but cannot review or amend the budget on a line-by-line basis. If the Police Services Board does not agree with the Council decision, it can appeal the decision to a provincially administered body.

### Debt repayment

Expenditures for interest and principal repayments of previously issued debt represent 4% of overall City expenditures. These repayments are for a fixed amount and time and it is not within Council's ability to adjust them during the yearly budget-setting process.

### Council-controlled expenditures

The remaining 58% of the City's expenses fall under City jurisdiction and the decision-making authority of City Council. These areas include:

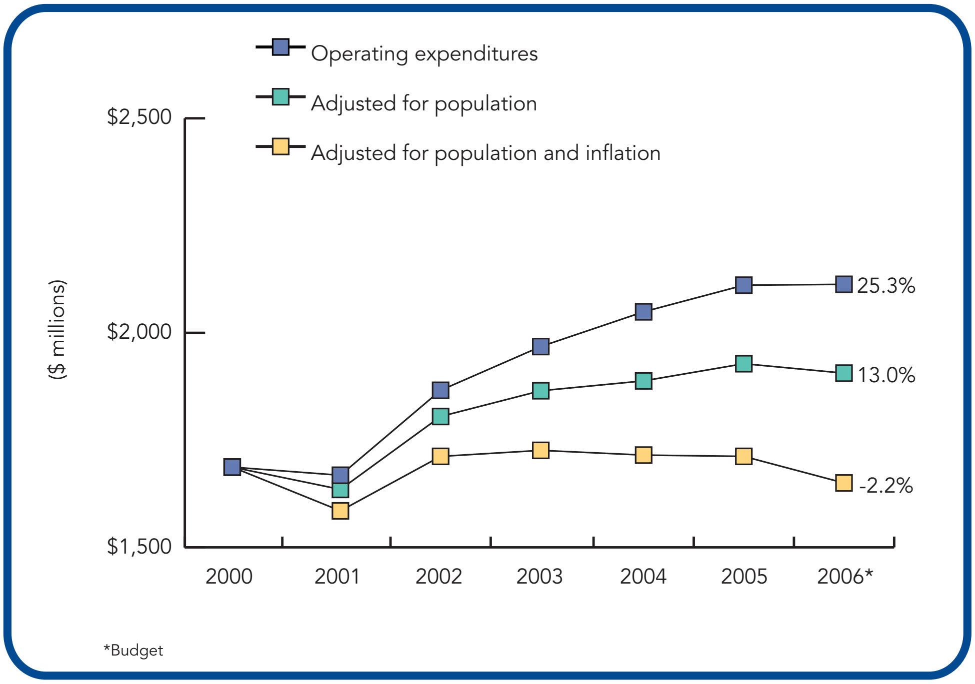
- Rate-supported programs: expenditures for the provision of potable water and sanitary/storm sewer services, funded by revenues from water and sewer surcharge rates.
- Tax-supported programs: expenditures for "traditional" municipal programs such as summer/winter road maintenance, public transit, fire services, garbage collection and parks and recreation. User fees are used to reduce the costs associated with some of these programs with the remainder funded through property taxes.
- Contribution to capital: yearly transfers to capital reserve funds to maximize cash financing of the City's tax- and rate-supported capital programs and minimize debt financing.

Unlike the Police Services budget, Council can approve expenditures for Library Services. The independent Library Board, composed of Councillors and appointed residents, proposes a budget that Council has the authority to review and adjust on a line-by-line basis. Library Services are therefore included under Council-controlled expenditures.

*Spending increases since amalgamation*

The City's operating budget has increased by 25.3% since amalgamation. When these increases are adjusted for increases in the population, the increase is 13%. When these increases are adjusted for both population increases and inflation, overall City spending has declined by 2.2%.

### City spending on operations




A review comparing Ottawa with Toronto, and the average of seven major Ontario municipalities, was conducted using the actual expenditures and revenues as reported in the 2005 provincially mandated Financial Information Return.

*How does Ottawa compare?*

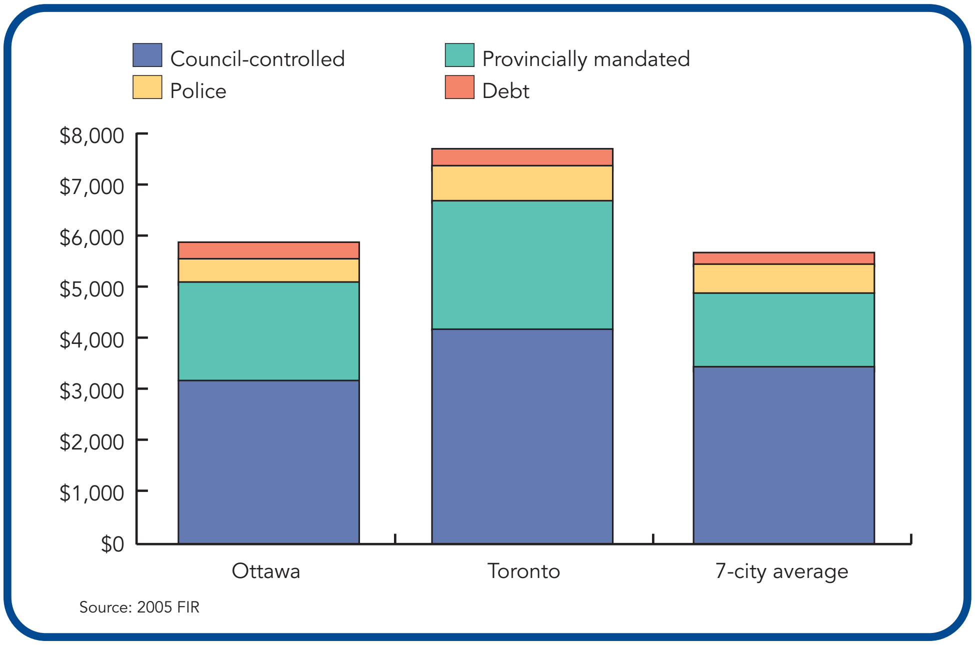
The seven Ontario municipalities included:

- Peel Region / lower tier municipalities
- York Region / lower tier municipalities
- Halton Region / lower tier municipalities
- Niagra Region / lower tier municipalities
- Durham Region / lower tier municipalities
- Hamilton
- London

When comparing total spending on a per household basis across the province, the City of Ottawa ($5,898) spends less than Toronto ($7,636), but slightly more than the seven-city average ($5,667). This type of peer-to-peer comparison of spending and revenue will be further broken down within this document.

### Total spending, per household, 2005

**By category**




## City services – Citizen Satisfaction Survey Report (EKOS Survey)

In 2004, as part of a new public consultation strategy for its revised annual budget process, City Council agreed to develop an annual residents' satisfaction survey. The goal was to produce a baseline measurement for tracking future changes and to provide Councillors and staff with additional information on a range of service- and policy-related issues.

The telephone survey included a random, representative sample of 1,000 residents (18 years of age or older), with a larger than typical proportion of residents in the rural areas to adequately represent each of four regions of the city. Survey results are considered to be accurate within three percentage points, 19 times out of 20.

The survey showed that while residents were pleased with City services and want to see them maintained or expanded, they do not want to pay more property taxes to maintain the current levels of service.

Produced by EKOS Research Associates, the survey report examined residents' satisfaction with City services, service priorities and funding options for services. The following 17 service areas were included.

| | |
|---|---|
| Fire Services | Social Housing and Shelters |
| Paramedic Services | Library Services |
| Police Services | Economic Development Services |
| Garbage and Recycling Services | Parking and Traffic Management |
| Road and Sidewalk Maintenance and Snow Removal | Land-use Planning, Zoning and Building Permits |
| Public Health Services | Child-care Services |
| Transit Services | By-law Services |
| Parks and Green Space Maintenance | Cultural Programs |
| Recreational Facilities and Programs | |

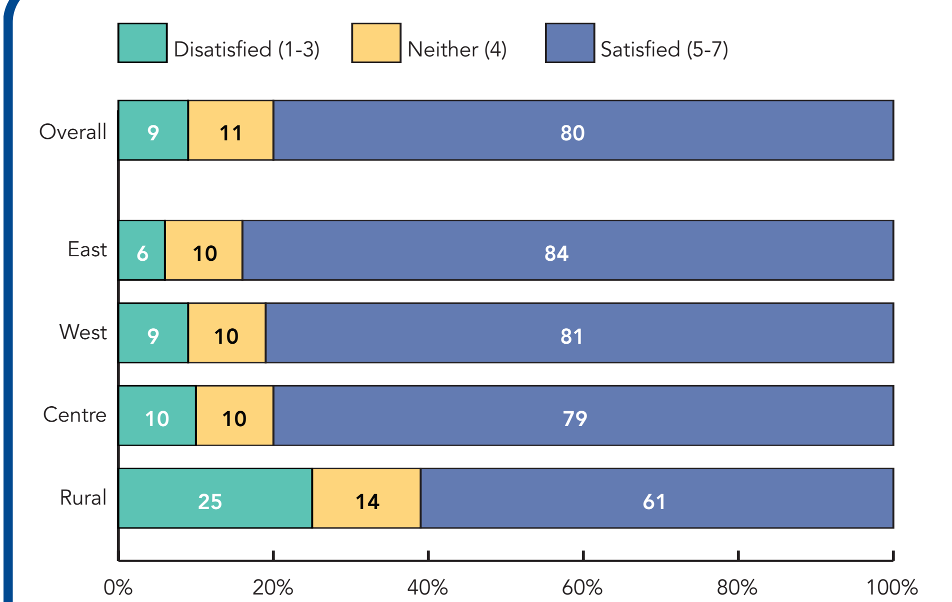
This survey resulted in three high-level conclusions.

***1) Residents were relatively satisfied with the performance of the City in providing services.***

Eighty per cent of Ottawa residents said they were satisfied with the overall level of service they received in 2004. Urban and suburban residents were more satisfied than rural residents. As a result of this survey, the City embarked on the 2005 Rural Summit process. There is now a City branch for Rural Affairs, with dedicated staff and many specific action items that are being implemented.

### Overall satisfaction with City services

**"Thinking more generally, how satisfied would you say you are with the overall services that are provided to you by the City of Ottawa?"**

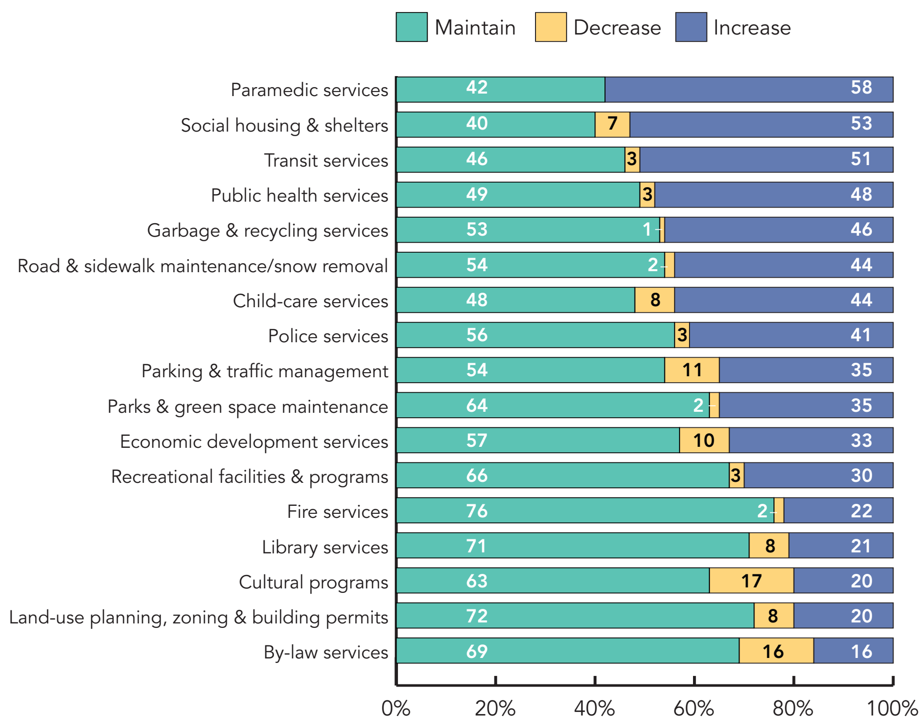



Source: City of Ottawa Citizen Satisfaction Survey 2004

*2) Residents value City services and want them maintained or expanded.*

The results showed clearly that an overwhelming majority of residents want services maintained or increased. Only a small minority of survey respondents felt that services should be reduced. Each of the 17 individual service areas examined in the study was considered to be important to a large majority of city residents. Emergency services topped the list, followed by garbage and recycling, road and sidewalk maintenance and snow removal, and public health. Virtually all residents indicated they would like to see the City increase or at least maintain current service levels in all 17 areas.

## Level of service



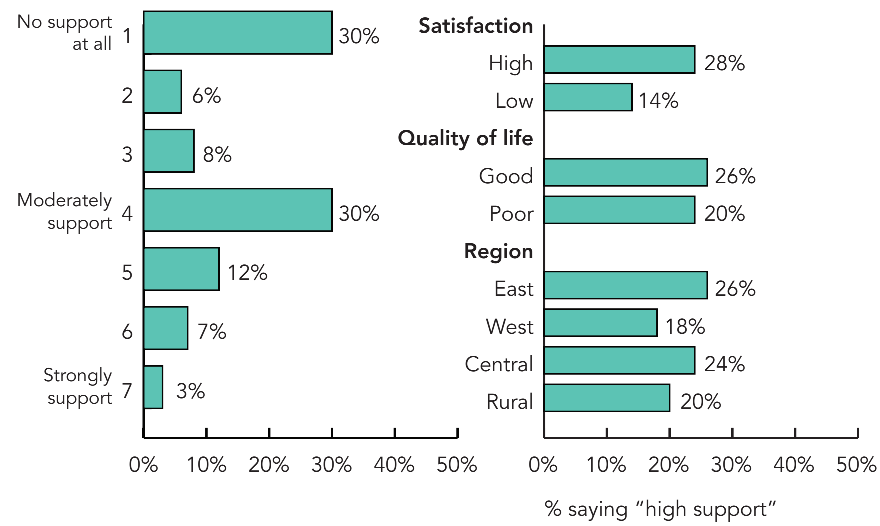

Source: City of Ottawa Citizen Satisfaction Survey 2004

*3) Residents do not want property taxes to increase.*

Despite high satisfaction with services and a desire to see spending on programs and services maintained, half of the respondents did not support a tax increase, while half only moderately supported the idea. This is not unexpected, but it points out a fundamental conflict between the value and importance of City services and the willingness to pay more to maintain current levels of service.

### Municipal tax rates

**"To what extent would you support an increase to your municipal taxes in order to fund the increased cost of delivering the same level of services that you have right now?"**




Source: City of Ottawa Citizen Satisfaction Survey 2004

## PROVINCIALLY MANDATED AND COST-SHARED PROGRAMS

The relationship between Ontario municipalities and the Province of Ontario has always involved programs that are primarily under the control of the provincial government, but are delivered, managed and partly funded from the municipal property tax base. While the Province establishes the service standards and policies for the vast majority of these programs, municipalities have limited discretion over the level of service provided, or the level of funding necessary to deliver these programs.

Under the 1998 Local Services Realignment process, the funding responsibilities for a number of new and existing program areas were either added or transferred to the municipalities or existing cost-sharing arrangements were changed.

Programs impacted by the 1998 process were:

- Employment and financial assistance
- Social housing
- Child-care services
- Long-term care
- Paramedic services
- Public health services
- Municipal Property Assessment Corporation (MPAC)

There has been a high growth rate of the City-funded portion of these programs since 1998.

### Provincial cost-sharing arrangements

Because the Province sets the standards and the cost-sharing arrangements, Council has minimal control over these mandated programs. As a result, these cost-shared programs increase the amount of property taxes paid by residents living in Ottawa.

In 2001, provincially mandated programs represented $565 of the average property tax bill. Today, if all provincially mandated/cost-shared programs were funded at the provincial level, the average urban residential household in Ottawa would pay $670 less in property taxes per year.

Very few programs are 100% funded by the Province. The cost-sharing arrangements between Ottawa and the Province, by service, are listed in the following table. The table also shows which program areas have a funding gap (the difference between the provincially mandated revenue as stated in the cost-sharing agreements, and the anticipated amount the Province will provide the City). For 2006, the funding gap is projected to be $16 million.

As an example, costs for Paramedic Services were transferred to the City in 1998; the cost-sharing agreement was to be on a 50/50 basis between the Province and the City, but only to the level of service that the Province established. In 2005, Ottawa City Council proactively increased the service standard for paramedic response times to above the level of service set by the Province. As a result, the additional costs required to meet these higher service standards are not being subsidized at the 50% level. Fortunately, in its 2006 Budget, the Province announced that an additional $300 million would be given to municipalities in an effort to move towards 50/50 cost-sharing for Paramedic Services over the next three years.[14]

The Province has also increased the funding for public health expenditures. Previously, the Province funded 50% of health expenditures. It moved to 65% in 2006, and will move to 75% in 2007. This additional funding has been used to reduce the net cost of providing health services, enhance existing services and meet increased service demands.

[14] MFOA 2006 Provincial Budget Highlights.

## Provincially mandated services

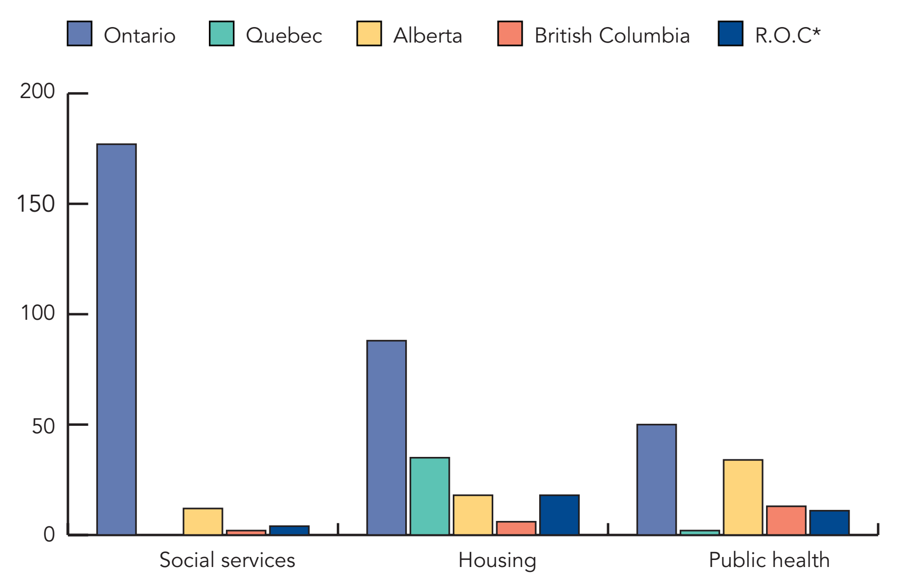
| Branch | Services | Mandated cost-sharing arrangements | Prov. revenue as mandated ($ thousands) | 2006 Budget revenue ($ thousands) | Funding gap ($ thousands) |
|---|---|---|---|---|---|
| **Paramedic services** | Emergency medical patient care | 50% | 22,416 | 18,579 | 3,837 |
| | Emergency medical dispatch | 100% | 5,567 | 5,567 | - |
| **Housing** | Residential & support services | 80% | 19,734 | 18,876 | 858 |
| | Housing programs adminstration | 0% | - | - | - |
| | Centralized waiting list (The Registry) | 0% | - | - | - |
| | Housing programs – rent supplement programs | 15% | 2,719 | 2,719 | - |
| | Public housing | 0% | - | - | - |
| | Affordable housing development | 45% | 160 | 160 | - |
| | Director's office | 0% | - | - | - |
| **Child-care** | Fee subsidy | 80% | 38,934 | 35,182 | 3,752 |
| | Ontario Works | 80% | 3,222 | 3,222 | - |
| | Wage subsidy, special needs, Early Years | 80% | 14,091 | 14,091 | - |
| | Pay equity | 83% | 2,320 | 2,320 | - |
| | Best Start | 100% | 6,557 | 6,557 | - |
| | Administration | 50% | 1,544 | 1,544 | - |
| **Public health** | Mandated programs | 65% | 19,570 | 18,536 | 1,034 |
| | Health protection (SARS, Smoke Free Ontario, Healthy Babies, etc.) | 100% | 8,172 | 8,172 | - |
| | West Nile | 65% | 543 | 543 | (0) |
| | Public health education & development | 65% | 742 | 543 | 199 |
| | Dental treatment | 0% | - | - | - |
| | Immunization program | 100% | 356 | 356 | - |
| **Employment & financial assistance** | Ontario Works & financial assistance | 80% | 111,638 | 111,638 | - |
| | Employment programs | 80% | 14,100 | 14,100 | - |
| | Essential health & social supports (EHSS) | 80% | 6,963 | 6,963 | - |
| | Home support programs | 80% | 1,818 | 1,568 | 250 |
| | Program delivery | 50% | 17,303 | 17,189 | 114 |
| | City-funded provincial programs | 80% | - | - | - |
| **Long-term care** | Nursing & personal care | 100% | 24,777 | 17,692 | 7,085 |
| | Program & support services | Funded on a per diem basis | 2,080 | 1,793 | 287 |
| | Food purchase | 100% | 1,386 | 1,386 | - |
| | Accommodation | 100% resident plus provincial minimum | 12,883 | 14,422 | (1,539) |
| | Outreach | 100% from the Province with user fee | 382 | 382 | - |
| **Total** | | | | | **15,877** |

*Ontario funds social services from property taxation*

Ontario is the only province in Canada to fund more than $3.5 billion of primarily social programs, like social services, social housing and public health, from the property tax bill each year. As seen in the graph below, municipal expenditures in Ontario, attributable to provincially mandated programs (after deducting conditional grants), are significantly higher than in any other province. As a result, municipal spending on programs funded from property taxation, such as social services, housing and public health, is $282 higher per capita in Ontario than in the rest of Canada.

The largest cost factor is social assistance, which requires Ontario municipalities to raise $173 more in taxation per capita than the rest of Canada.[15] Other Canadian provinces simply do not fund these social programs through property taxes, resulting in much lower municipal costs and lower property taxes. Ontario municipalities have argued for many years that income redistribution programs, such as social assistance, should not be funded from property taxes – a regressive tax that is not reflective of the income level of a property owner. Rather, these programs should be linked to and funded more appropriately from provincial income taxes.

**Municipal expenditures (after conditional grants) on provincially mandated services, per capita**




"Ontario's Municipalities in the Fiscal Imbalance", Kitchen, Harry M., Trent University

* Rest of Canada minus Ontario

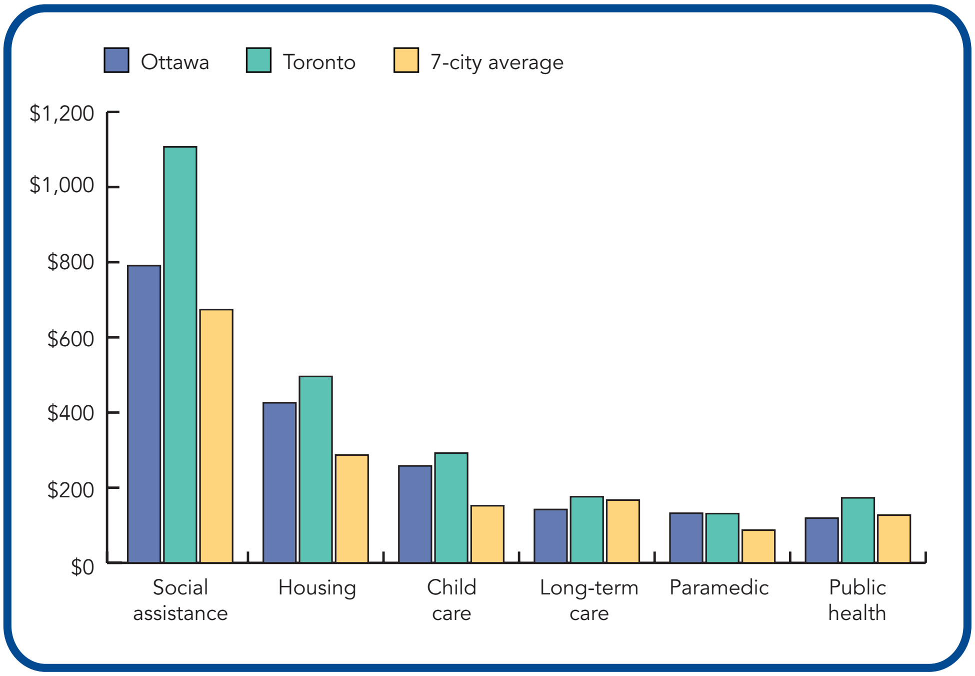
Because Ontario is the only province to have a major portion of the costs for these items funded from the property tax bill, comparisons between property taxes in Ontario and other provinces are not valid.

[15] Kitchen, Harry M., "Ontario's Municipalities in the Fiscal Imbalance," Trent University. 2006.

*Ottawa spending compared to other Ontario cities*

The graph below compares Ottawa's 2005 gross costs (before grants or user fees) by household, for provincially mandated programs, with Toronto and the seven-city average.

**Comparison of provincially mandated programs, per household**



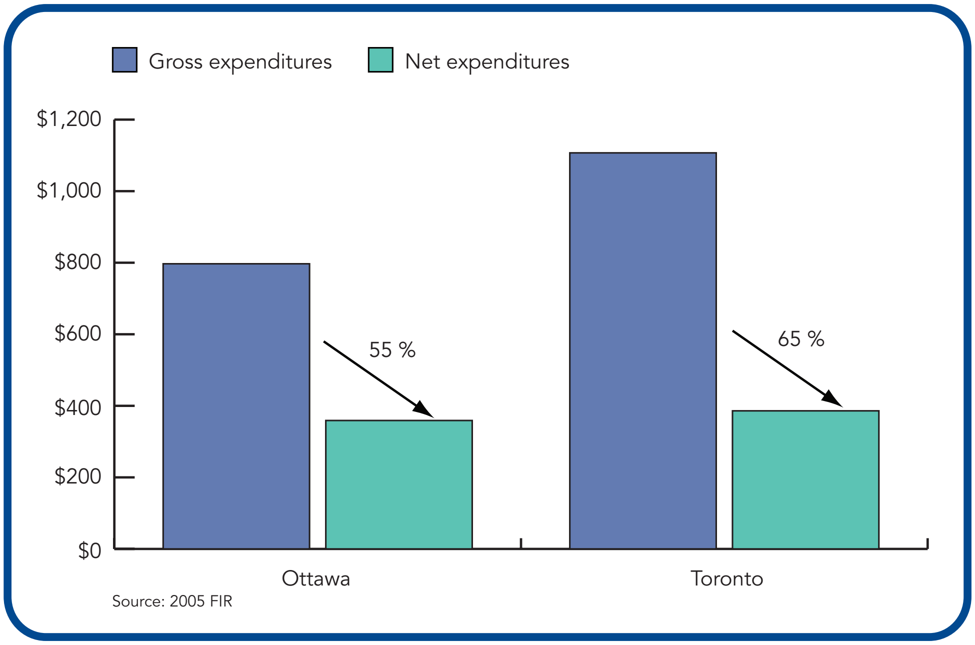

When compared to Toronto, Ottawa spends less per household on all programs except for the paramedic program. Because Ottawa City Council has proactively improved paramedic services, spending for this service, on a per household basis, is equivalent to Toronto.

Ottawa spends more than the seven-city average for all programs except long-term care and public health. This is to be expected since large urban areas are typically employment centres that generally tend to have more social services available, thereby attracting people looking for work and for assistance. The seven cities used in the comparison are smaller, suburban centres clustered around Toronto. As a result, most of the demand for social services is focused in Toronto itself.

*Social assistance costs more on the Ottawa tax bill*

While Toronto spends more, per household, on social assistance than Ottawa, the two cities are fairly comparable when looking at the net expenditure for the program.

## Social assistance expenditure comparison




Toronto is able, through grants and subsidies from the Province and other municipalities, to reduce its gross program costs by 65%. Ottawa is only able to reduce the amount by 55%.

Toronto, unlike Ottawa, benefits from a provincially imposed Greater Toronto Area equalization formula, which pools social assistance and social housing costs, in the GTA area. The Province created this program for Toronto because its costs were higher than the average. This allows Toronto to receive funds from other GTA municipalities to compensate for its social assistance and social housing expenditures.

In 2005, this equalization formula saved Toronto taxpayers $189 million in taxation. Like Toronto, Ottawa's social assistance and social housing costs are also higher than the provincial average; however, Ottawa is not included in any type of pooling with surrounding municipalities. For illustrative purposes, if Ottawa were to be included in the GTA pooling, Ottawa residents would be relieved of $53 million in taxation per year.

The Province recently revised the Social Program Grant component in the Ontario Municipal Partnership Fund (OMPF). These grants are allocated to municipalities with high social costs relative to their residents' household incomes. By basing the grant on household income, the Province recognizes that income transfer programs, such as welfare, should be funded from income taxation and not property taxation. Ottawa will receive $6 million in OMPF grants in 2006 or approximately 3% of social program expenditures. Toronto, on the other hand, will receive $34.9 million, representing 6% of its social program costs. If Ottawa residents were to be treated the same as Toronto residents, the grant would be $12 million.

*MPAC costs have increased beyond inflation*

The provincial Municipal Property Assessment Corporation (MPAC) administers a uniform, Ontario-wide property assessment system for municipalities. Assessment values are used to calculate the amount of tax a property is charged.

Since 1998, Ontario cities have been required to pay a share of the cost of MPAC based on a combination of the number of properties and their assessed values. The cost of the Corporation is not within the control or influence of Council and is completely funded from taxes. Ottawa's share of the cost of the assessment service has increased by almost $2 million since amalgamation, representing an overall 25% increase, or 5% per year, well above the City's tax increase or the rate of inflation. For 2006, the cost of MPAC to the City is approaching $9.8 million.

### Next steps: Provincial-Municipal Fiscal and Service Delivery Review

On August 14, 2006, Ontario announced its intent to strengthen its relationship with municipalities by launching a joint review aimed at improving the delivery and funding of municipal services for Ontario families. The Provincial-Municipal Fiscal and Service Delivery Review will be conducted by both levels of government over the next 18 months. A public report will be released in the spring of 2008.

Some of the areas that may be examined include:

- Delivery and funding of housing, health and social services
- Municipal financing tools, such as user fees and the use of municipal debt
- Infrastructure funding
- The Ontario Municipal Partnership Fund

Taxing powers, such as income tax and sales tax, will not be included in the review.

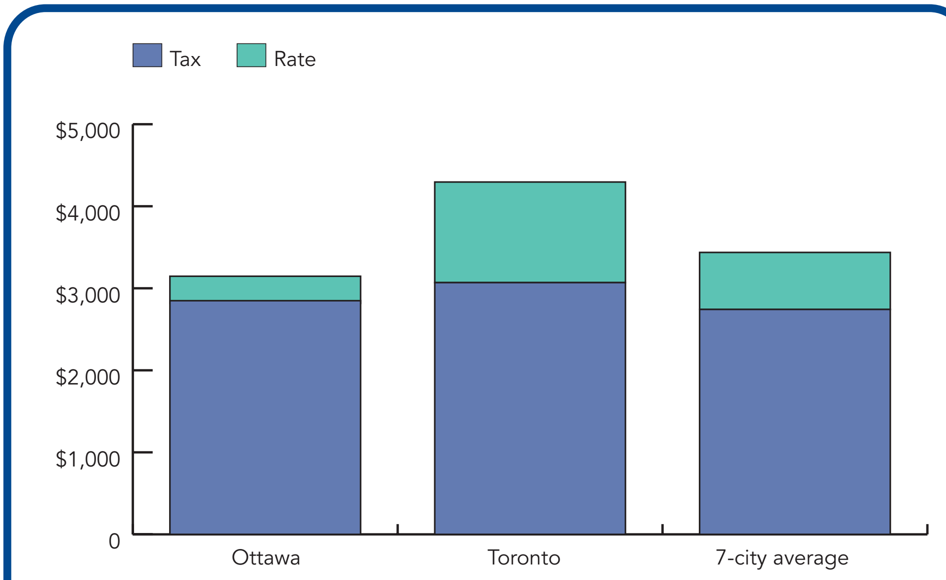
The Association of Municipalities of Ontario (AMO) has agreed to join in this initiative to allow the Province and the municipal sector to improve the delivery and funding of services for Ontarians. Together, the partners will examine how Ontario communities can prosper through initiatives such as better service delivery and improved infrastructure investment.

The joint review flows from the provincial government's plan to strengthen local government in Ontario. The plan includes the proposed *Municipal Statute Law Amendment Act, 2006*, which, if passed, would provide new powers and more flexibility to municipalities. Both partners have indicated their determination to investigate and deliver long-term sustainable options for the province and the municipal sector that are affordable to both levels of government.

## COUNCIL-CONTROLLED PROGRAMS

Ottawa's Council directly controlled 58% of the total gross 2006 budget, amounting to $1,217 million in gross expenditures or approximately $3,184 per household, as seen in the graph below. Overall, in 2005 Ottawa spent $1,052 less than Toronto and $223 less than the seven-city average primarily because of lower spending on water and sewer programs. Details on the various Council-controlled programs follow.

### Total Council-controlled spending, per household

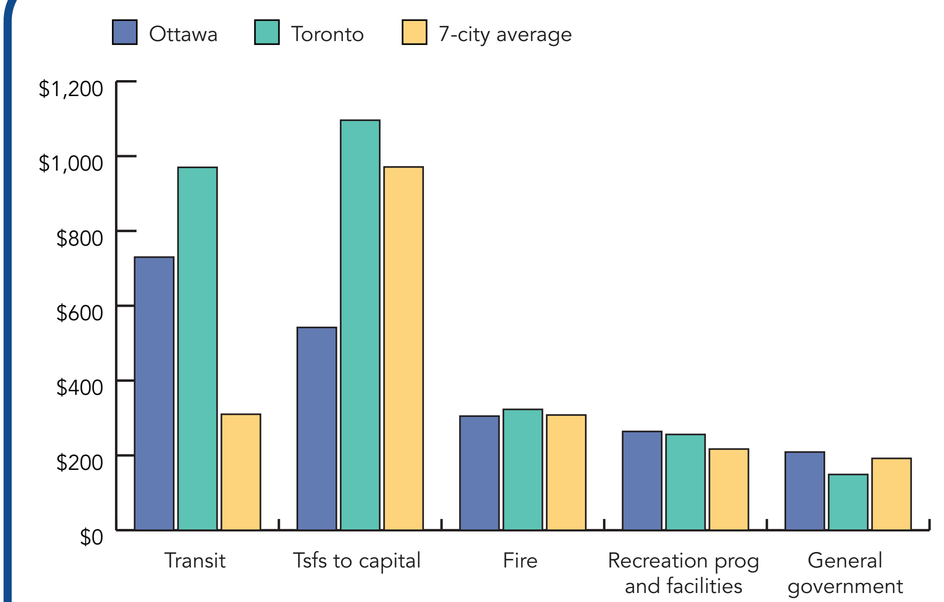



Source: 2005 FIR

In 2005, the five most expensive Council-controlled programs, on a gross per household basis, were transit services, transfers to capital, fire services, recreational programs and facilities, and general government. The spending comparisons for these areas are shown in the following graph.

*Ottawa's spending is comparable to major Ontario cities*

### Per household spending comparisons, 2005




Source: 2005 FIR

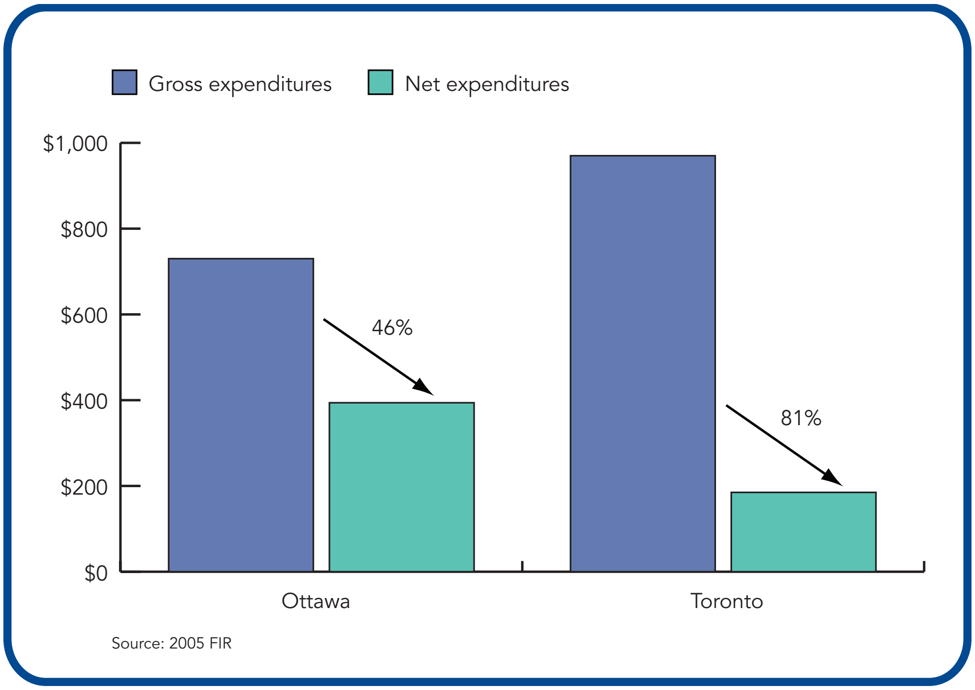
Transit services are Ottawa's largest Council-controlled gross expenditure. Ottawa spends approximately $730 per household on transit services. This is significantly higher than the seven-city average, which includes municipalities without extensive public transit systems. However, Ottawa spends less than Toronto, on a per household basis for transit, which would be expected, given the Toronto transit system's size and the number of riders.

As shown below, Toronto's net expenditure for transit is much less than Ottawa's, for several reasons. For example, Toronto is able to recover 81% of its transit costs from user fees and provincial grants, with the largest portion coming from user fees. In 2005, Toronto's user fees covered 72% of the cost. The same year, Ottawa's user fees covered only 45% of the direct operating costs. Ottawa City Council has since adopted a policy to collect 55% of direct operating expenditures from user fees.

In addition, Toronto is able to use its entire provincial gas tax allocation to pay transit operating costs whereas Ottawa only uses a portion of it for growth-related operating costs. Toronto is able to use all of the provincial gas tax for operating costs as they receive more capital transit grants than Ottawa; therefore, they do not need to use the provincial gas tax for capital costs.

The Province of Ontario stopped providing transit operating grants in 1997. Ottawa must now fund 54% of transit service costs from the property tax bill, while Toronto only has to fund 19%.

### Transit services expenditure comparison



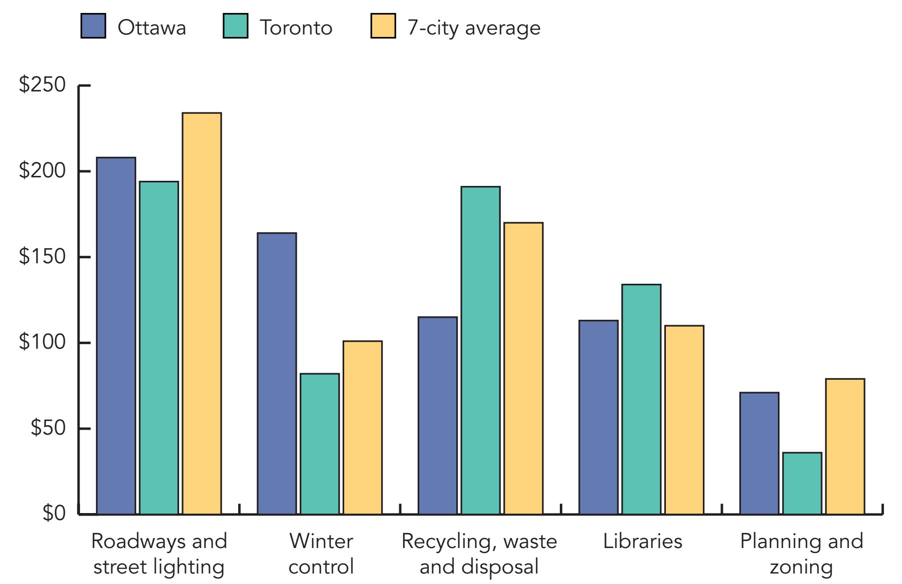

Ottawa's second largest Council-controlled expense is transfers to capital. These are annual transfers to capital reserve fund accounts, to be used to cash finance capital expenditures. Ottawa currently spends less per household than Toronto and the seven-city average on transfers to capital. Lower spending on tranfers to capital reflects Ottawa's decision to fund more capital projects with debt than other municipalities. When debt servicing is added to the contribution to capital for tax-supported capital projects, Ottawa's spending is higher than Toronto's and approximately 15% less than the seven-city average. However, Ottawa's overall expenditures will likely rise in the future since Council has approved a policy to increase contributions to capital by the rate of the Infrastructure Construction Price Index as calculated by Statistics Canada.

Fire services, and recreational programs and facilities are the next largest expenditure in Ottawa. City spending is similar to Toronto's and the seven-city average for these services.

Ottawa's general government expenditures, which include functions such as Council, the City Manager's office, the Deputy City Managers' offices, the Auditor General, the City Clerk's office and Client Services and Public Information, are slightly higher than Toronto's and the seven-city average. Unlike the other cities, Ottawa uses a "centre of expertise" organizational structure. As a result, costs that would normally be found in individual branches in a decentralized organization are allocated to the general government category. Toronto and the seven cities have not generally adopted this centralized approach, which explains why Ottawa's costs appear to be higher.

The remaining major service costs controlled by Council are shown in the following graph. These include roadways and street lighting, winter control services, recycling, waste and disposal services, libraries and planning and zoning services.

### Per household spending comparisons, 2005




Source: 2005 FIR

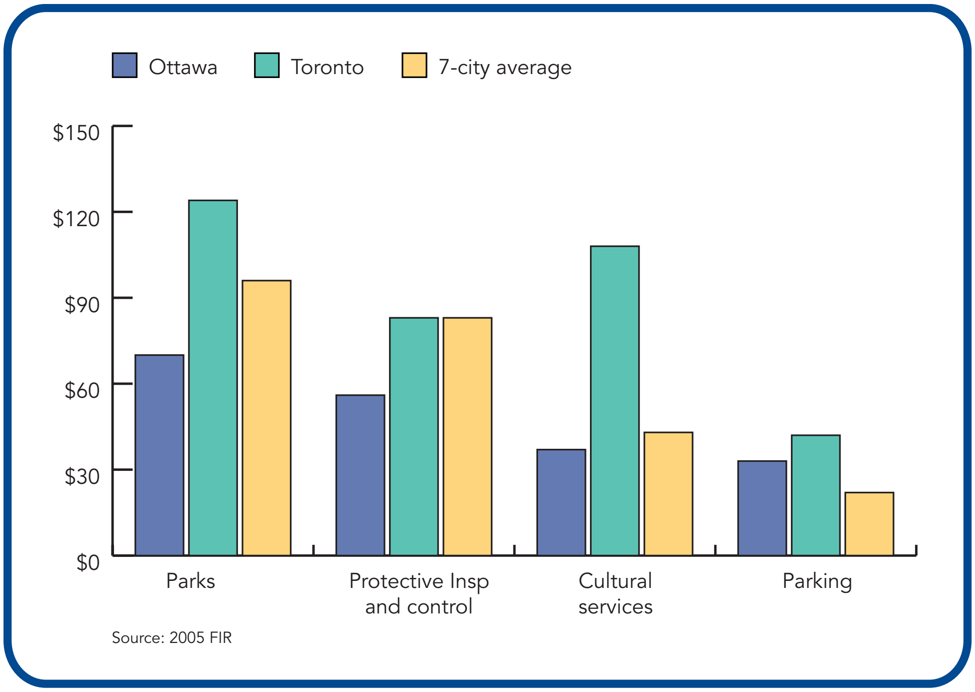
Ottawa's costs for roadways and street lighting – approximately $208 per household – are similar to, but slightly higher than Toronto's costs, and lower than the cost in the seven-city average. Winter control spending in Ottawa (snow ploughing and removal), is approximately $164 per household, which is higher than Toronto and the seven-city average. This reflects the differences in climate (more snow and freezing rain) and geography, as well as differing service decisions in the various municipalities.

With four disposal sites across the city (two privately operated and two City-operated), Ottawa spends much less for recycling, waste and disposal than Toronto, which has no local disposal facilities and therefore incurs greater shipping costs to dispose of its waste.

Spending per household on library services, and land planning and zoning services is fairly equivalent between Ottawa, Toronto, and the seven-city average. Because Toronto is more developed, its spending on planning services is slightly lower than that of the growing cities in the seven-city average.

Council also controls expenditures for parks, protective inspections and controls, cultural services and parking. Household spending comparisons are shown in the following graph.

### Per household spending comparisons, 2005




Source: 2005 FIR

Ottawa spends less than Toronto and the seven-city average on parks, protective inspection and controls, and cultural services. Parking expenditures per household are between Toronto's and the seven-city average.

At approximately $37 per household, Ottawa's cultural services costs are comparable to the seven-city average. Toronto spends far more on cultural services. In 2003, Toronto adopted the "Culture Plan for the Creative City," which provides for spending in cultural services to dramatically increase over five years, with a $2 per capita increase annually.[16]

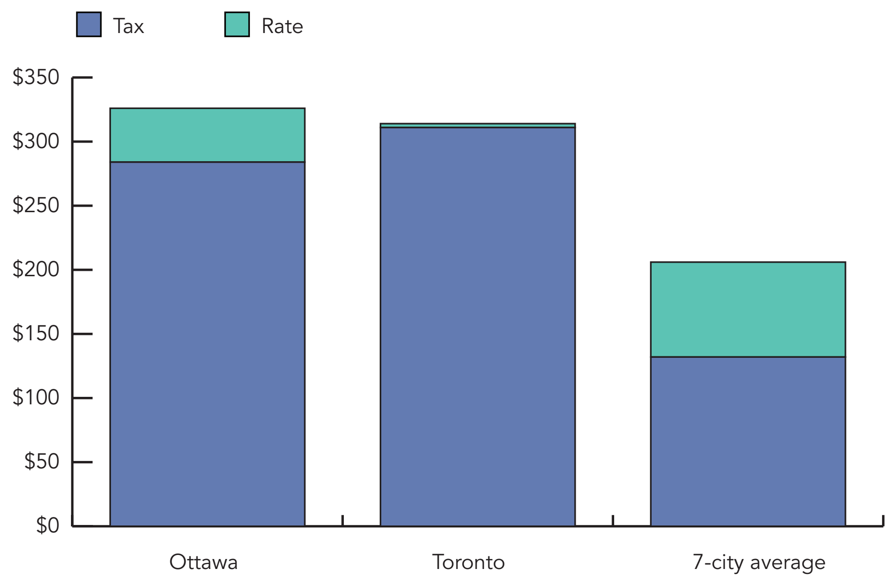
In 2006, Ottawa City Council endorsed the creation of an Arts Investment Steering Committee to help position Ottawa as a competitive, creative city. The Committee, which is investigating investment strategies to close the revenue gap for Ottawa's local arts and festival sector, is expected to present its report to Council before the end of 2007.

## Management of debt

Another program controlled by Council is the management of debt. As seen in the following graph, Ottawa spends approximately $326 per household on debt charges, including principal and interest payments on liabilities such as the issuance of debt (debentures), term bank loans and sinking funds. These debt repayment charges are funded from taxation and the water/sewer bill. Long-term debt finances municipal capital projects within the City.

[16] "Cultural Plan for the Creative City," City of Toronto, 2003, pg. 6.

## Per household debt spending comparisons, 2005




Source: 2005 FIR

Since 2001, the Long-Range Financial Plan process (LRFP I and II) has been used to assess the capital infrastructure needs to help meet the projected lifecycle and population growth requirements of the city. To achieve Council goals, LRFPs employ a combination of financing tools, including development charges, funding from other levels of government, transfers from the capital reserve funds and the issuance of debt.

### *Why the City uses debt financing*

Since provincial legislation does not permit municipal governments to finance operating deficits through debt, the City only borrows money for capital works such as roads, water and sewer systems, buildings and transit projects.

Council requires that capital assets financed by debt have a useful life at least as long as the term of the debt. The actual terms and structure of debt financing vary with market conditions; however, debt is generally issued for 10 or 20 years. Longer debt terms are sometimes undertaken for capital programs with substantially longer useful lives such as the Light Rail Transit project. When required, debt is considered an appropriate way of financing longer-life items since future taxpayers who benefit from the project pay for it through future debt charges. To achieve the lowest borrowing costs, the City usually seeks debt financing in the Canadian public financial market.

The City has adopted the practice of maintaining tax-supported debt charges within a “budget envelope.” Thus, as older debt matures, new debt is issued and the amount of debt charges (principle and interest repayments) collected through taxes remains relatively constant.

Since amalgamation, the City has benefited from lower interest rates and issued new debt at much lower interest rates than in earlier years. This has allowed the City to service more debt at a lower cost. As shown in the following table, the cost of tax-supported debt as a percentage of the tax requirement has fallen significantly since amalgamation.

### Tax-supported debt compared to the net tax requirement, $ thousands

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|
| Tax-supported debt charges | 70,927 | 72,524 | 65,135 | 65,206 | 74,336 | 67,695 | 72,561 |
| Total property tax revenues | 746,521 | 777,859 | 805,484 | 826,484 | 864,494 | 919,747 | 953,498 |
| Cost of tax-supported debt as percentage of tax requirement | 9.50% | 9.30% | 8.10% | 7.90% | 8.60% | 7.40% | 7.61% |

The next table shows that total issued net debt[17] is expected to increase over the next four years to $912 million. This increase aligns with the recommendations adopted in LRFP II, and is largely due to the increase in gas tax and other revenue-supported debt. Approximately $196 million of the projected $912 million stems from debt issued for the Light Rail Transit project. The debt will largely be paid through financing from other levels of government and development charges.

### Net issued debt by revenue source, $ millions

| | 2006 | 2007 | 2008 | 2009 | 2010 |
|---|---|---|---|---|---|
| Tax-supported | 469 | 471 | 463 | 463 | 466 |
| Rate-supported | 73 | 96 | 123 | 144 | 170 |
| Other revenue-supported | 0 | 125 | 242 | 260 | 276 |
| Total | 542 | 692 | 828 | 867 | 912 |

*City debt servicing is well below provincial limits*

The Province regulates the amount of debt municipalities issue by setting an annual repayment limit for each municipality. This is the maximum amount by which a municipality may increase its debt and other financial obligations in the following year. The repayment limit is set at 25% of a municipality's net own-source revenues, including taxation, user fees and any other non-provincial or federal funding. The repayment limit imposed by the Province on the City of Ottawa is $293 million – representing the maximum amount of debt charges (principal and interest repayments) to be incurred annually. This would allow the City to issue up to $3.1 billion in new debt depending on the terms and conditions of the debt.[18]

Although Ottawa's current and projected debt is well below the provincial limit, if it were to reach the limit, future operating budgets would be severely constrained or tax and other revenues would have to increase significantly.

[17] Net debt is defined as the total debt outstanding less the amount of any sinking funds. For certain types of debentures, the *Municipal Act* requires the City to set aside a sum of money each year, which will accumulate to the total principal amount of the debenture payable on maturity.

[18] The provincial limit sets the maximum amount available to service debt charges. Thus the amount of new debt that could be issued will vary with the term selected and the interest rates at the time.

The City of Ottawa is not alone in forecasting rising levels of debt due to long-term capital expenditures. A research report on the finances of Canadian municipalities issued by Standard & Poor's in May 2006 states that:

> "across all rating categories and steadily since 2001, debt and debt burdens have been increasing…it is increasingly evident that rated municipalities are overcoming their historical aversion to debt as they address their substantial infrastructure deficiencies."

The difference in Ottawa is that future increases in debt are to be funded from non-tax sources of revenue, thereby ensuring that the City's taxation remains fairly flexible.

## OTTAWA POLICE SERVICE FINANCES IN CONTEXT

Every Canadian municipality providing police services reports that these costs constitute one of the biggest financial commitments in the annual budget and resulting tax rate. The Ottawa Police Service (OPS) represents 16% of the total 2006 City property tax bill, excluding education – $404 for an average residence with an assessed property value of $276,245. On a cost-per-service basis, transit is the only City cost exceeding the cost of policing.

The Ottawa Police Service gross budget has increased in the past few years; increases can be attributed mainly to added costs for contract personnel and growth in the number of officers required. Gross annual budget increases since amalgamation in 2001 are presented in the table below.

### OPS gross budget, 2001 to 2006

| | 2001<br>$ thousands | 2002<br>$ thousands | 2003<br>$ thousands | 2004<br>$ housands | 2005<br>$ thousands | 2006<br>$ thousands |
|---|---|---|---|---|---|---|
| OPS operating budget – total gross expenditures* | 128,761 | 137,130 | 144,279 | 158,427 | 174,670 | 189,167 |
| % Annual increase | | 6.5% | 5.2% | 9.8% | 10.3% | 8.3% |

* Gross expenditures excluding non-operational costs

As presented in the next table, while gross spending has increased over this period, most increases have been proportional with the total City budget. Since 2003, the proportional police share of the total City budget has increased from 7.8% to 9%.

### OPS gross budget in proportion to total City budget

| Gross operating budget | 2001<br>$ thousands | 2002<br>$ thousands | 2003<br>$ thousands | 2004<br>$ thousands | 2005<br>$ thousands | 2006<br>$ thousands |
|---|---|---|---|---|---|---|
| City operating budget | 1,681,519 | 1,726,046 | 1,838,862 | 1,898,290 | 1,988,385 | 2,113,224 |
| OPS operating budget* | 128,761 | 137,130 | 144,279 | 158,427 | 174,670 | 189,167 |
| OPS as % of total city | 7.7% | 7.9% | 7.8% | 8.3% | 8.8% | 9.0% |

* Gross expenditures excluding non-operational costs

Even with proportionately greater increases in recent years, OPS spending compares favourably with other municipalities in Ontario. For example, spending on police services in Toronto represents 10%[19] of gross municipal spending.

The most recent police costs published by Statistics Canada in 2005 show that, on a per capita basis, Ottawa falls in the middle of a selection of 12 Canadian municipalities.

### Police costs, per capita

| Service | Cost ($) | Rank |
|---|---|---|
| Toronto | 284 | 1 |
| Vancouver | 282 | 2 |
| Edmonton | 257 | 3 |
| Montréal | 236 | 4 |
| Calgary | 231 | 5 |
| **OTTAWA** | **204** | **6** |
| Peel | 199 | 7 |
| Hamilton | 196 | 8 |
| Durham | 189 | 9 |
| Gatineau (Urban) | 169 | 10 |
| Halton | 165 | 11 |
| York | 163 | 12 |

Source: "Police Resources in Canada," 2005. (Statistics Canada, 85-225). Based on 2004 population and 2005 policing costs.

Population per police officer is another common measure published annually by Statistics Canada. The most recent statistics from 2004 show that Ottawa falls close to the low end of the ranking, with 1 police officer for every 771 residents.

### Population, per police officer

Source: "Police Resources in Canada", 2005. (Statistics Canada, 85-225). Based on 2004 population and 2004 police officers.

| Service | Ratio | Rank |
|---|---|---|
| Montréal | 482 | 1 |
| Toronto | 492 | 2 |
| Vancouver | 520 | 3 |
| Edmonton | 566 | 4 |
| Calgary | 640 | 5 |
| Peel | 690 | 6 |
| Hamilton | 708 | 7 |
| Gatineau (urban) | 711 | 8 |
| Durham | 757 | 9 |
| **OTTAWA** | **771** | **10** |
| Halton | 843 | 11 |
| York | 867 | 12 |

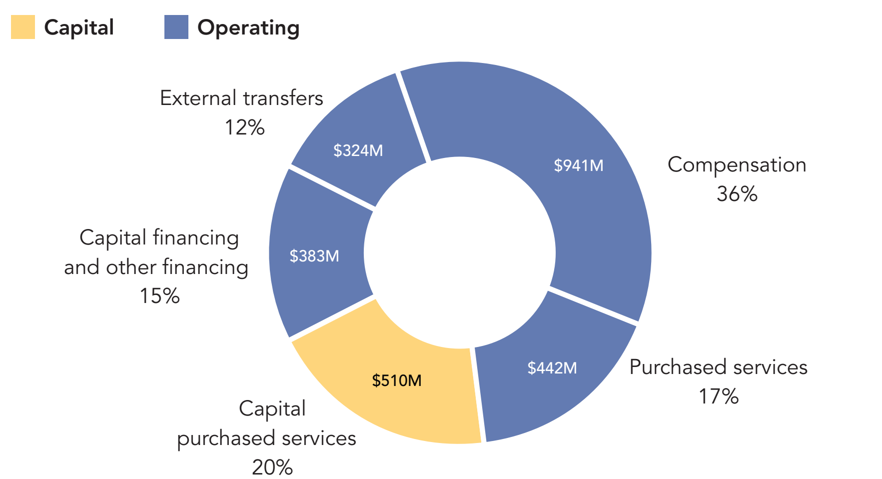
The Ottawa Police Service Strategic Staffing Initiative (SSI) has helped increase the number of sworn officers by 90 since 2004. In 2006, there are 1,251 sworn officers in Ottawa serving a population of 870,250 – one police officer for every 695 residents.

[19] City of Toronto.

## OVERVIEW OF SPENDING BY EXPENDITURE TYPE

As reported in the provincially mandated Financial Information Return (FIR), Ottawa's total operating and capital expenditures in 2005 amounted to $2.6 billion. The graph below shows that combined purchases of operating and capital purchased goods and services amounted to $952 million, or 37% of total expenditures. The next largest expenditure, at $941 million or 36% of expenditures, was compensation, which includes salaries, wages and employee benefits. Of the remaining expenditures, 15% were for capital financing, including contributions to capital and debt financing, and 12% for external transfers, including social assistance, housing subsidies, child-care subsidies, cultural grants and payments to conservation authorities.

### Total operating and capital expenditures, 2005
**($2.6 billion)**



Source: 2005 FIR

## COMPENSATION

Compensation costs represent the single largest component of the City's operating budget. Managing compensation costs is one of the most challenging issues for Ottawa and other large Canadian municipalities for a number of reasons:

- A highly unionized workforce and collective bargaining settlements that are often beyond the rate of inflation put real pressure on municipal budgets.
- Unions continue to negotiate for stronger benefits packages, while the City is grappling to pay for increases in the cost of providing existing benefits that far exceed the Consumer Price Index.
- Wage settlements are heavily influenced by settlements across Ontario, particularly in the Toronto area. Increases in compensation costs may also be influenced by settlements imposed by provincial arbitrators.

- The City of Ottawa is the second largest employer in the city, after the federal government, and must compete against other levels of government and the private sector for resources in the same talent pool. Attracting employees with similar education and work experience requires that salaries and benefits packages remain competitive.

## Employment figures at the City of Ottawa

The number of Full-Time Equivalent positions (FTEs) at the City changes every year in response to increased demand for services from a growing population, implementation of new programs by Council or changes to provincial legislation.

For example, the City had 13,003, 12,755 and 13,139 FTEs for 2003, 2004 and 2005, respectively. These numbers include the Ottawa Police Service and the Ottawa Public Library and represent positions, not employees.

A single FTE can represent more than one position if the positions are casual or part-time. For example, a part-time position in Parks and Recreation may be equivalent to 0.08 FTEs; a seasonal position in the Public Works department (e.g., involving the operation of snow-clearing equipment) could equate to 0.4 FTEs; and a full-time public health nurse would be 1.0 FTEs. Therefore, multiple employees can be associated with one FTE.

The City manages scheduling and payment of wage employees on an hourly basis. For budget purposes, the yearly total of wage employee hours, or wage pool, is converted to FTEs. However, the type of work performed and the associated hourly rates vary seasonally and annually, especially during changeovers in the spring and fall.

Each summer, there is a significant increase in the number of employees due to the student employment program. The total number of employees is also influenced by factors such as resignations, retirements and completion of temporary work terms. These variations mean that the total number of employees is much higher than the total FTE count, and more importantly, that the number is not static.

On average, 17,000 employees work for the City each year. In 2006, the total number of employees varied from a low of 16,135 in January to a high of 17,675 in July; the number of FTEs, on the other hand, remained relatively constant over that period.

Council's Delegated Authority By-law places strict controls on the number of FTEs at the City. Council must approve any increase to the total number of FTEs for both full- and part-time work. Monthly reports showing current FTEs and the total number of employees at the City allow Council to track changes.

## Employee compensation

Total spending on compensation, including the Ottawa Police Service, was $913 million in 2004, and $941 million in 2005. In addition to base salaries, employee compensation includes elements such as:

- One-time compensation payments awarded as retroactive collective agreement settlements
- One-time cost adjustments for items such as pay equity or reclassifications
- All premiums (governed by collective agreements)
- One-time compensation costs as a result of grievances or arbitration decisions
- Benefits costs

Excluding these elements, base salaries paid to City employees totalled approximately $673 million in 2004 and $706 million in 2005.

*How Ottawa compensation costs compare to other municipalities*

The majority of municipal employees are unionized. Pay scales for unionized positions are set through collective agreement(s) and the job evaluation process. Changes to a position's base salary range are negotiated as part of collective bargaining. Annual increases at the City of Ottawa are comparable to those in other large municipalities. The table below compares wage settlements for the City of Ottawa's unionized groups with wages in a selection of other municipalities.

### Economic increases, by municipality (largest union), 2001-2005

| Municipality | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| **Ottawa** | **2.50%** | **2.75%** | **3.00%** | **3.00%** | **3.00%** |
| Mississauga | 2.50% | 2.50% | 2.50% | 2.50% | 3.00% |
| Calgary | 3.50% | 3.50% | 3.00% | 3.50% | 3.50% |
| Edmonton | 3.00% | 3.00% | 3.00% | 3.50% | 3.50% |
| Brampton | 2.50% | 2.50% | 2.50% | 2.50% | 3.00% |
| Winnipeg | 2.50% | 2.00% | 3.00% | 3.00% | 3.00% |
| Hamilton | 2.00% | 2.00% | 3.85% | 2.83% | 2.25% |
| London | 2.30% | 2.30% | 3.00% | 3.00% | 2.90% |
| Vancouver | 2.50% | 2.50% | 2.50% | 3.00% | 2.50% |
| Toronto | 3.20% | 3.00% | 3.00% | 3.00% | 2.75% |
| Durham | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% |
| Niagara | 2.00% | 3.00% | 3.00% | 3.00% | 3.00% |
| Halton* | 3.00% | 9.00% | 2.50% | 4.90% | N/A |
| York | 2.10% | 2.20% | 2.90% | 3.00% | 3.00% |
| **Average** | 2.62% | 3.12% | 2.90% | 3.13% | 2.95% |
| **Median** | 2.50% | 2.50% | 3.00% | 3.00% | 3.00% |
| **75th percentile** | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% |

*Large increases approved to facilitate a change in market position.

A number of factors influence salaries paid to City employees:

- The scope of responsibilities and the specific job duties of the position
- The education, experience, certification and knowledge required to qualify for the position
- Whether the position is unionized
- Whether the pay grade for the position is influenced by the City's pay equity plan
- Whether exceptional market demand for the experience, education, skills or training required for the job results in problems attracting and retaining qualified candidates

The City monitors salaries and benefits and compares them to similar positions at public and private sector organizations in Ontario and across Canada. Overall, results for Ottawa compare favourably to other municipalities.

*Many management positions are compensated below the median rates*

Current and past surveys and studies conducted by local and national compensation specialists, such as Mercer Human Resources Consulting, indicate that unionized City positions tend to pay the same as or slightly better than those in the private sector. However, the surveys also show that some specialized technical positions, as well as many management positions, are compensated below the median rates paid in the public and private sectors. This trend becomes more pronounced at more senior levels within the organization.

Comparisons to other large municipalities provide one perspective on how Ottawa's salaries fare. However, the City of Ottawa hires the majority of its employees from the local labour market, and therefore compensation must compete with that offered by other employers in the area, particularly the federal government.

In 2005, Council set a policy to limit pay increases for the management and professional exempt group to increases in the Ottawa Consumer Price Index. The intent was to send a clear message to residents and City unions that Council was concerned about budget pressures associated with compensation costs. The City has a policy that management salaries should be within the 75th percentile when benchmarked against other major Canadian cities, including Brampton, Mississauga, Hamilton, London, Windsor, Calgary, Edmonton, and the Regions of Durham, Halton, Niagara, Peel, Waterloo and York. Management salaries were at the 75th percentile in 2002. The City is awaiting 2006 Mercer survey results for current data on management salaries.

Approximately 95% of the City's workforce is unionized. Amalgamation reduced the number of collective agreements inherited from the former municipalities from over 50 to 11, not including the Ottawa Police Service.

## The impact of collective bargaining

Ottawa's largest bargaining agent is the Canadian Union of Public Employees (CUPE), which represents six groups for a total of more than 8,000 City employees:

- CUPE Local 503 – Inside/Outside workers
- CUPE Local 503 – Library
- CUPE Local 503 – Part-time (Recreation and Culture)
- CUPE Local 5500 – Transit Fleet Maintenance
- CUPE Local 5500 – Transit Supervisor
- CUPE Local 5500 – Transit Security

The other five bargaining agents include:

- Amalgamated Transit Union (ATU) Local 279
- Amalgamated Transit Union, Local 1760
- Civic Institute of Professional Personnel (CIPP)
- Ottawa Professional Fire Fighters Association (OPFFA), and
- International Alliance of Theatrical Stage Employees (IATSE), Local 471

There are collective agreements in place for all of these groups, covering terms from one to three years, with staggered expiry dates. Therefore, the City is almost always in active collective bargaining with one or more of these groups.

Each collective agreement covers three areas:

- Wages
- Benefits
- Working conditions

City Council approves the negotiating mandate prior to any discussions regarding monetary issues in the collective bargaining process. While the City makes every effort to negotiate an agreement at the bargaining table, there are instances when this cannot be achieved. Most of the bargaining groups at the City have binding arbitration as the dispute resolution mechanism. The exceptions to this include ATU 279, CUPE 5500 and CUPE 503 Library, which have strike provisions in their collective agreements.

Binding arbitration preserves the operation of City services if the parties cannot reach a new agreement, and prevents work stoppages that could result if a strike provision were included in these collective agreements.

The City's experience shows that arbitration does not necessarily produce higher settlements than those negotiated at the collective bargaining table or through strike action. In general, wage settlements at the City are comparable to those in other large Ontario municipalities.

The table below depicts the wage settlements for bargaining groups at the City of Ottawa since amalgamation and compares them to the CPI.

## Collective agreement settlements, new City of Ottawa

| Year | MPE | CUPE 503 (Inside/ Outside) | Civic Institute of Prof'l Personnel | ATU 279 | ATU 1760 | CUPE 5500 | CUPE Library | Part Time Rec & Culture | Fire | IATSE | Police – Civilians | CPI Ottawa | CPI Ontario | CPI Canada |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **2008** | | | | | 3.00% | | | | | | | | | |
| **2007** | | | | 3.00% | 3.00% | 3.00% | | | | | | | | |
| **2006** | 2.30% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% | 2.75% | 3.00% | | | 2.96% eff. inc.** | | | |
| **2005** | 2.20% | 3.00% | 3.00% | 3.00% | 2.20% | 3.00% | 2.25% | 3.00% | | | 3.640% | 2.3% | 2.2% | 2.2% |
| **2004** | 2.50% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% | 3.00% | | 3.00% | 3.632% | 1.9% | 1.9% | 1.9% |
| **2003** | 3.00% | 1. 3.00%<br>2. Harmonize | 1. Harmonize<br>2. 2.50%<br>3. 6th step added | 3.00% | 3.00% | 3.00% | 2.50% | 2.75% eff. inc.** | 4.47% eff. inc.** | 2.75% | 3.885% | 2.5% | 2.7% | 2.8% |
| **2002** | 2.50% | 2.75% | 1. 3.60% lump sum – T4 earnings<br>2. 5.00% | 3.00% | 2.75% | 3.00% | Harmonize | 1. 2.00% lump sum (Jan-Aug)<br>2. 2.00%<br>3. Harmonize rates | 3.31% eff. inc.** | 2.50% | 3.33% eff. inc.** | 2.2% | 2.0% | 2.2% |
| **2001** | 2.50% | 2.50% | 3.60% lump sum - T4 earnings | 2.00% | 2.50% | 2.00% | 3.00% lump sum | 3.00% lump sum | 1. Harmonize<br>2. 2.5% | | 2.51% eff. inc.** | 3.2% | 3.1% | 2.6% |
| **2000** | 2.38% eff. inc.** | 2.25% eff. inc.** | 2.38% eff. inc.** | 2.00% | N/A | 2.00% | 1 | 1 | 1 | 1 | 2.52% eff. inc.** | 3.0% | 2.9% | 2.7% |

Notes
1. Function not at the regional level - owned by the amalgamating municipalities.
* Collective agreements can be effective throughout the calendar year.
** Effective increase (eff. inc.) indicates where there has been more than one pay increase applied in a calendar year (e.g., one in January and one in July). In scenarios such as this, the second pay increase must be compounded onto the first pay increase.

Like other Ontario municipalities, Ottawa must often accept wage decisions made by arbitrators where it is clear that the amount of the increase is directly related to awards made in the Greater Toronto Area. The significant costs that result for the City from this practice are particularly evident in agreements for fire, police and ambulance workers across Ontario.

Employee benefits are the second major compensation cost for the City.

The City has taken several steps since amalgamation to control the escalating costs of providing and administering benefits, including:

*Benefits costs are rising*

- Consolidating benefits with fewer providers to reduce administrative overhead and administrative costs
- Implementing self-insured long-term disability coverage rather than using an external provider, to reduce annual costs
- Externally administering self-insured benefits to lower administration costs
- Negotiating similar benefits in collective agreements to reduce the complexity and cost of providing benefits
- Minimizing the number of additional benefits negotiated into collective agreements

Despite gains from these measures, all employers across Ontario have experienced hyper-inflationary increases in the cost of providing benefits. At the time of amalgamation in Ottawa, the average cost of providing employee benefits was about 15% of base salaries. This cost has increased to nearly 23.5%, primarily to cover increases in basic premiums. Specific payments such as long-term disability costs have increased by 42% during this period.

Benefit costs also include the employer's share of the Ontario Municipal Employee Retirement System (OMERS) pension plan. At the time of amalgamation, a contribution holiday was in effect for both employers and employees. Premiums were later reintroduced and the OMERS Board approved an increase to the current level of 6.5% for earnings up to the yearly maximum pensionable earnings (currently $42,100) and 9.6% on earnings above that threshold for employees with a normal retirement age of 65. Employers must match the employees' premiums.

The decision to move to a self-insured model for long-term disability was a direct result of the significant cost increase in providing this benefit through an external insurance carrier between 2005 and 2006.

Several major factors have influenced staffing level changes since amalgamation. Reductions in staffing levels have occurred because of amalgamation savings and Universal Program Review while legislated and mandated changes and population growth have increased staffing levels.

Prior to amalgamation, the 12 former municipalities' total FTE count was 12,786. Since then, Ottawa has reduced the number of FTEs in all program areas. FTE savings attributed to amalgamation took place primarily within a three-year period, and yielded a reduction of 665 FTEs, or 5.2% of the original number of FTEs of the amalgamated city.

## *Changes in City staffing since amalgamation*

In 2004, the Universal Program Review and corporate reorganization resulted in an additional reduction of 483 FTEs, or 3.8% of the original number of employees. A similar exercise in 2006 yielded a further reduction of 88 FTEs.

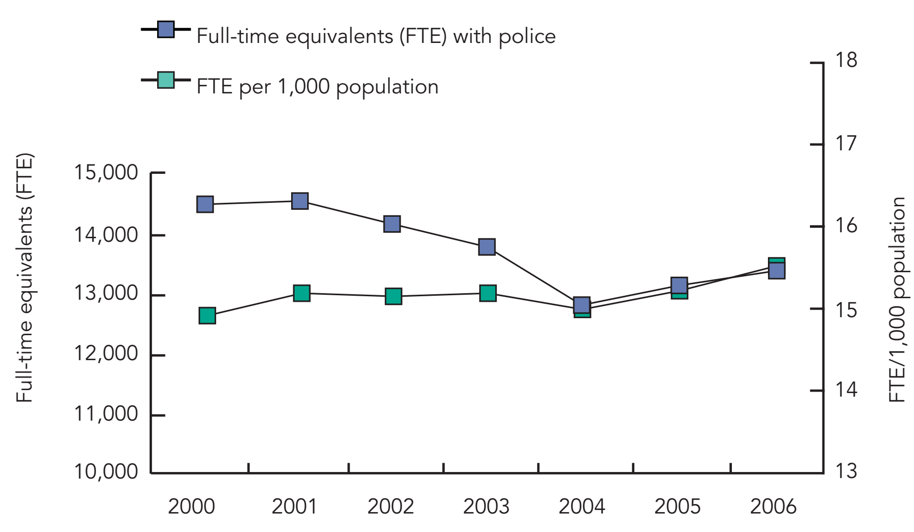
From 2001 to mid-2006, provincially and federally funded programming, as well as legislated and mandated changes, increased the number of FTEs by 586, or 4.6% of the original complement. Major changes included the provincial downloading of paramedic services (388 FTEs) and provincially funded housing, long-term care and public health programs (108 FTEs).

The City of Ottawa has also experienced significant growth in population and infrastructure since amalgamation. As a result, 1,332 FTEs have been added, or 10.4% of the original complement. Key contributors include growth in public transportation affecting transit services and fleet services (376 FTEs) and the Police Service's Strategic Staffing Initiative (310 FTEs).

The net effect of these changes is an overall increase in FTEs since amalgamation of 682 (which includes 306 additional Ottawa Police Service FTEs), or 5.3% of the 2000 year-end complement, which were approved by City Council.

The graph below reflects the effect of these changes. While staffing levels have risen slightly over the period, there has been an overall decline in staffing levels per thousand residents since 2000. In 2000, there were approximately 16.2 FTEs for every thousand residents; in 2006 there are 15.5 FTEs for every thousand residents.

### Staffing levels

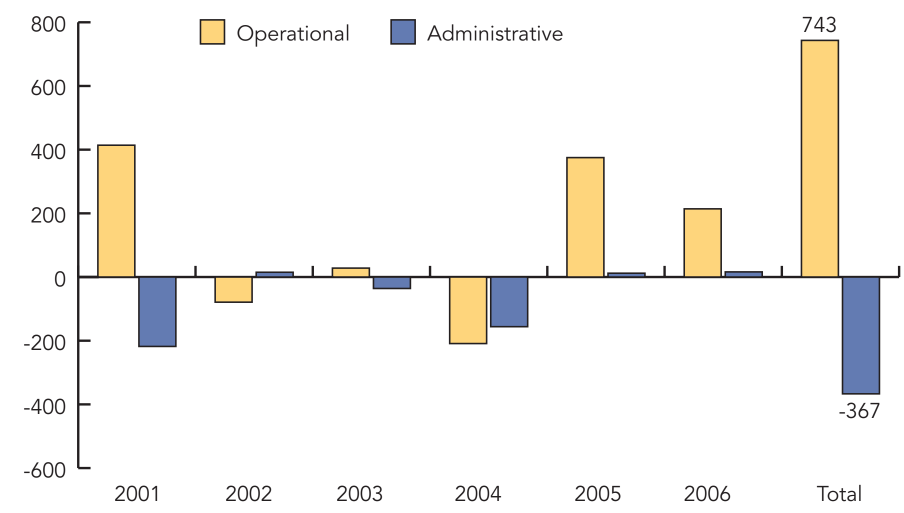



Source: City of Ottawa, August 2006

The increase of 682 FTEs since amalgamation includes 306 FTEs for Police Services. If the Police increases are removed, the remaining increase of 376 FTEs can be split into administrative and operational positions. Overall, there were 743 operational positions created and 367 administrative positions eliminated over the 2001 to 2006 time period.

The graph below represents the changes in operational and administrative FTEs since amalgamation, excluding police.

### Change in the FTEs per year, operational vs. administrative
**(as of August 15, 2006)**




Source: City of Ottawa

In 2005, the City of Ottawa's first Human Resources (HR) Plan was tabled with Council. The Plan reported on FTE allocations and forecast future requirements based on operational needs. It also provided information about the resourcing of key City functions. The next HR Plan will be tabled in 2007 in conjunction with the City of Ottawa's budget process.

## PURCHASED SERVICES AND MATERIALS

### The City ensures the best price through competition

The City has more than 17,000 employees, covers a geographic area of 2,796 square kilometres, and owns hundreds of buildings ranging in age from one to a hundred years. Therefore, there are very few types of goods and services that are not needed by the City of Ottawa. To support its varied needs, the City routinely purchases:

- Construction services related to all types of civil infrastructure, roads, sewers, and bridges, and construction related to City-owned facilities

- Fleet services, including all classes and types of vehicles, replacement parts, snow removal services, sewer maintenance, roadway sweeping, grass cutting and garbage removal services
- Goods, including computer hardware and software, copiers and printers, electrical, plumbing and hardware equipment, office products and fine paper, telephone and radio systems, traffic control systems, medical and dental supplies, uniforms, parks and recreational equipment, trees, sod, road salt, water treatment chemicals, etc.
- Consulting services, including expertise in fields of engineering, architecture, planning and environmental studies, and legal services

*The City has a comprehensive purchasing by-law in place that requires services and goods to be purchased through a competitive process*

The City has a comprehensive purchasing by-law in place that requires services and goods to be purchased through a competitive process. In 2005, the City issued nearly 700 formal bid solicitations for goods or services, each exceeding $100,000 in value, with a total contract value of $1.021 billion. Of these, 98% were awarded either to the lowest bidder or to the proposal that represented best value. The 2% that did not go through the competitive process were primarily for non-competitive services, such as local utility-type monopolies.

The City is able to leverage its position as a major consumer of goods and services to obtain best value. Some of its procurement strategies include:

- Two- or three-year contract terms that challenge bidders to provide the most competitive long-range business plan, in return for the economic benefits of a substantial contractual commitment with the City, allowing employment and supply chain decisions to be maximized.
- Extension options to continue purchasing a known, satisfactory service, often with a minimal cost increase.
- Incorporation of Ontario Ministry of Transportation formulas that allow fuel price escalation during the life of the contract. For example, this means that the Greater Ottawa Trucking Association and others who provide snow removal and garbage collection are able to submit accurate bids that are not inflated to reflect possible fuel price increases.
- Forward contracting for commodities subject to significant price volatility, such as diesel fuel. Locking in diesel fuel prices in July 2005 avoided over $1.5 million in price increases since then.
- Buying natural gas through the Ottawa Carleton Energy Purchasing Group (OCEPG), comprising 17 local organizations associated with the Municipal, Academic, School Board, Hospital (MASH) sector. The City has saved 7.3%, or $360,000 per year, thanks to this arrangement.

The City also minimizes the amount of stock held in inventory, using a just-in-time purchasing approach that sets minimum stock levels based on projected workload or demand. The City's inventories were valued at $23.4 million at the end of 2005. Approximately $86 million in materials and goods flow through the City's warehouse/stores each year.

The City also minimizes consumption of goods through such policies as "no idling" to reduce fuel consumption. Salt usage guidelines minimize the amount of road salt applied, and temperatures in City buildings are set higher in summer and lower in winter than in past years. All of these efforts promote responsible management of service costs.

## OPERATING RESERVES

Municipalities ensure that essential services like water, sewer, snow clearing, emergency response and many others are reliably available to residents year-round. There are years, however, when municipalities face unanticipated and unavoidable costs in delivering these services. In Ottawa, for example, unpredictable and severe winter conditions and the possibility of emergency situations can affect yearly spending.

Cities establish operating reserve funds, similar to a household "rainy day" fund, to cover these unforeseen costs and to avoid having to resort to tax increases in any given year. For example, some cities create an insurance claims reserve to cover the cost of claims that exceed the yearly budgeted amount. Reserves are typically funded from budget surpluses or through regular contributions from the operating budget.

Municipalities also require funding for special "one-time-only" projects or programs that are only active for a short period. For example, Ottawa's elections reserve is funded through a yearly tax contribution and used every four years to cover municipal election costs.

At amalgamation, the City of Ottawa created operating reserve funds with combined balances of approximately $54.5 million. Since then, these funds have been used, as designed, to mitigate funding pressures that would have otherwise resulted in service reductions or deferrals, or higher property tax increases.

The City of Ottawa has five operating reserves to offset expenditure fluctuations:

- Self-insurance
- Vested benefits
- Tax stabilization
- Elections
- Winter maintenance

With the exception of the elections reserve, which is funded from a yearly tax contribution, the remaining reserves are funded from budget surpluses or one-time, Council-approved funding.

Because provincial law dictates that municipalities must table balanced budgets – unlike the two other levels of government – a budgeted deficit is not allowed. The Tax Stabilization Reserve was established at amalgamation to cover expenses that cannot be forecast. This reserve, which is funded from previous year surpluses and any special contribution Council decides to make, can be drawn upon if the City incurs a deficit in any given year.

At the end of 2005, Ottawa had $13.1 million in operating reserves. Rather than directing more funds to the reserves, Council has instead adjusted the budget every year to try and ensure that sufficient funds are available to continue to provide appropriate levels of service. For example, when the winter maintenance reserve was depleted in 2002, Council increased the winter maintenance budget to reflect the average spending of the past three years. This increased funding should reduce the City's need to resort to reserves and absorb potential increased costs due to weather.

It is prudent financial management to either adjust the budget or replenish operating reserve funds each year. Because the municipality cannot incur a deficit, the only other source of funds is the city-wide capital reserve fund. Yearly contributions are made to this reserve fund from property tax revenues to provide funds to cash finance the City's capital program. However, repeated withdrawals from this reserve reduce the City's ability to fully fund priority capital projects in the following year.

## PERFORMANCE MEASUREMENT

Given the constraints on municipalities' ability to continue to meet service and infrastructure demands with existing funding mechanisms (the fiscal imbalance), it will soon become nearly impossible for cities to deliver all of the services they currently provide with only property tax and user fee increases to fund them. Council and City staff must have new tools to continuously improve services and to decide whether investments are yielding the anticipated results.

The new performance measurement and reporting framework the City adopted in early 2006 provides such a tool. It will lead to more and better information for managers and decision-makers, enhanced public accountability and, ultimately, improved performance. The performance measurement framework will allow the City to measure progress against plans, as well as to measure performance year over year, compare performance to service standards and measure performance against other Ontario municipalities.

These are the key components of the performance measurement and reporting framework.

### The Ontario Municipal Benchmarking Initiative (OMBI)

Ottawa reports performance-related information to the provincial government through mandatory programs such as the Ontario Municipal Performance Measurement Program (MPMP) and the Financial Information Return (FIR). However, these measures represent only a small portion of City services. Ottawa also participates in the Ontario Municipal Benchmarking Initiative (OMBI), which draws upon base MPMP information and supplements it with additional data on municipal services. OMBI describes services from four perspectives:

- Community impact
- Service level
- Efficiency
- Customer service

OMBI currently involves 15 large Ontario municipalities that share information on approximately 600 performance measures across 33 program areas. By comparing performance data with other Ontario municipalities, OMBI allows Ottawa to benchmark its performance in various areas. This in turn helps the City identify and share best practice information, and apply what is learned to continuously improve service delivery and business processes.

When the City participated in OMBI for the first time in 2005, 22 program areas were reviewed and it reported on approximately half of the 500 performance measures. In 2006, the City is participating in all 33 program areas and will report on many of the performance measures by the end of 2006.

Finding valid (i.e., "apples-to-apples") comparators is a significant undertaking, given the differences in geography, demographics, services and service levels among Ontario municipalities. To that end, municipal program area managers are encouraged to participate in the OMBI subject matter expert working groups to ensure that the chosen performance indicators are meaningful, data definitions are appropriate, data analysis results are valid, and best practices are shared.

### Annual Report

The City of Ottawa's annual report provides a performance overview for the previous year. The annual report sets out:

- The City's main goals
- The status of action items in the City Corporate Plan and departmental business plans
- High-level performance information for key programs and activities

The City's first annual report, in 2004, included audited financial statements and analysis as well as an overview of the City's key achievements. The 2005 annual report, issued in June 2006, provides enhanced information on the City's progress in achieving both the priorities set through the Ottawa 20/20 consultations and the desired outcomes identified in the 11 agendas in the City Corporate Plan.

### Quarterly performance report to Council

Beginning in fall 2006, the City will provide Council with a quarterly report containing high-level metrics and information about the City's performance in major service areas. The goal of the report is to provide key measures for a cross-section of branches that deliver public services of high interest to Councillors. Over time, it is expected the report will change to incorporate Council's evolving areas of focus, and to include more performance measures. Ultimately, the quarterly performance report will provide information on 50 to 75 performance measures for up to 15 different branches.

The City is also developing a business intelligence and reporting application that builds on existing information systems such as SAP to produce real-time performance information. This application will allow managers to respond faster to emerging issues and quickly identify improvement areas.

Developing effective performance measurement systems takes time: time to design, time to implement and time to perfect. The City of Ottawa's performance measurement framework is in its early stages, and components are still being developed and perfected. Once complete, it will be a key tool that will support priority setting by Council, and will foster the City's continuous improvement culture by identifying where resources should be invested and operations enhanced.

## LIABILITIES (EXPENSES) INCURRED FOR SERVICES PROVIDED IN FUTURE

Some of the expenses, or liabilities, the City incurs do not have to be paid immediately. For example, the City could enter into a contract with a union to provide benefits to members after they retire. This liability would increase every year until the union members retired.

Since 2000, municipalities have been required to prepare their financial statements in accordance with accounting policies set out by the Public Sector Accounting Board (PSAB), an independent body with the authority to set accounting standards for the public sector. The 12-member governing board comprises federal, provincial and local government accountants, auditor generals, public auditors, budget officials and academics. PSAB's mission is to set standards and provide guidance for public sector financial and other performance information.

Under PSAB policies, employee benefits must be recorded in financial statements at the time they occur, as a liability to be paid in the future.

The City's employee benefits liability is made up of four categories: post-retirement benefits, post-employment benefits, Worker Safety Insurance Board (WSIB) obligations, and vacation leave. Post-retirement benefits include health care, dental care and life insurance. Post-employment benefits are made up of accumulated sick leave payouts and continuation of benefits while an employee is on long-term disability.

PSAB deems each of these categories to be employee benefits, and all must be reviewed to determine the ongoing liability to the City. This liability is shown as employee benefits in the liabilities section of the City's Consolidated Statement of Financial Position (see page 60 of the *2005 City of Ottawa Annual Report*).

The City funds post-employment and post-retirement benefits on a cash basis. As a result, employee benefits are included in the budget as the value of the payments to be made in a given year. As the City's workforce ages and retires, the cash payments for these benefits are steadily increasing, which will cause significant budget pressures in the future.

To lessen the impact of these future budget increases and ensure that those who receive the services today pay the full cost, the City is developing a 10-year plan to move from a cash basis to an accrual accounting basis for these liabilities. With this plan, the liability will be paid out of the budget in the year it is incurred rather than the year it is paid out. If the City does not implement such a plan, significant budget increases will be required in the years when these liabilities have to be paid.

### Landfill closure liability

The City of Ottawa provides garbage collection and disposal services to residents and businesses and operates two landfill sites for this purpose. When these sites reach capacity and are closed, the City will continue to be responsible for their ongoing maintenance under the *Ontario Environmental Protection Act*. Post-closure care for these sites (and other inactive sites) is expected to last approximately 25 years. The PSAB requires the City to record the estimated liability in its financial statements.

In 2005, the value of this future cost was estimated to be $10.8 million; this figure will increase every year until the landfills close. Based on the principle that those benefiting from the landfill today should pay for its future closing costs, City Council has included a provision for landfill closure and post-closure costs as part of the new user-pay structure for solid waste management.

# PART B: REVENUES

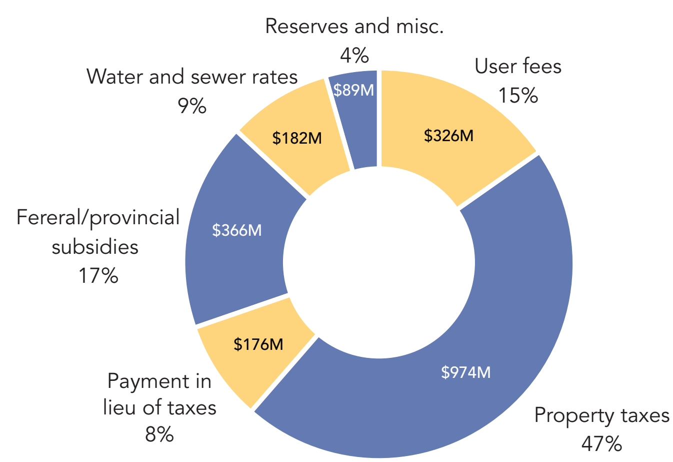
## Revenue overview

The City of Ottawa has five main revenue sources to fund the operating budget.

1. Property taxes – In 2006, the City budgeted $974 million in property tax revenue and $176 million for payments in lieu of taxes to fund 55% of the total operating budget.
2. Government grants – At $366 million, grants from the federal and provincial governments fund 17% of the operating budget.
3. User fees – This revenue comes directly from residents using the many services the City offers. Ottawa plans to collect $326 million in 2006 to fund 15% of the operating budget.
4. Water and sewer rates – These represent $182 million and fund 9% of the total City operating budget.
5. Reserve funds – Transfers from City reserves and other miscellaneous revenues fund 4% of the operating budget.

### Breakdown of operating revenues

**2006 operating budget ($2,113M)**




Source: City of Ottawa

# TAXATION

Economic and policy experts agree that Canada's cities lack the legislative and financial tools needed to fund the services and programs they must deliver. They also agree that rectifying this situation is essential for Canada's economic prosperity.

This situation has been an ongoing concern for the City of Ottawa and for Canada's other large cities. Until the inadequacies of the fiscal framework are addressed, no Canadian city will be sustainable in the medium- to long-term, no matter what it does to reduce its own costs or increase its own revenues.

As experts Enid Slack and Richard Bird noted in May 2006:

> "Owing to the limited and relatively inelastic revenue base to which even the largest cities have access, the underlying basis of Canada's urban prosperity is being eroded, with potentially damaging implications for national well-being over the long run."[20]

There are only three funding tools available to cities — property tax, user fees, and development charges — and property tax is the only tax available to municipalities. Property tax has

*Experts agree City revenues are inadequate*

> "characteristics that make it different from other taxes… [It] is an inelastic tax… because property values do not grow as quickly as do incomes and sales during a period of economic growth…Even when they do grow quickly….most municipalities are forced to reduce tax rates when property values increase so that taxes do not increase by the full amount of the increase in the tax base".[21]

It is generally agreed that "property tax has insufficient revenue-generating capacity to meet increased expenditure needs."[22]

Moreover, as Enid Slack notes:

> "… the ability of municipalities to increase taxes and user fees is different than the ability of federal and provincial governments to increase their revenues for at least two different reasons. First, municipalities are constrained by provincial governments in terms of the services that they are mandated to deliver, on the one hand, and the restrictions on revenues they are permitted to levy, on the other hand. Second, the unique characteristics of the property tax make it more difficult to increase than income and sales taxes."[23]

Ontario municipalities are further disadvantaged by having to fund income redistribution programs from the property tax base. Studies show that Ontario's decision to download social services to municipalities "mak[es] no real sense."[24]

[20] Slack, Enid and Bird, Richard M. "Cities in Canadian Federalism." Presentation. Conference on Fiscal Relations and Fiscal Conditions. Georgia State University, Atlanta. May 2006.
[21] Slack, Enid. "Fiscal Imbalance: The Case for Cities." June 1, 2006.
[22] Kitchen, Harry M. "Financing Canadian Cities In The Future?" May 21, 2004.
[23] Slack, Enid. "Fiscal Imbalance: The Case for Cities." June 1, 2006.
[24] Slack, Enid and Bird, Richard M. "Cities in Canadian Federalism." Presentation. Conference on Fiscal Relations and Fiscal Conditions. Georgia State University, Atlanta. May 2006.

Studies also note that many municipalities appear, on the surface, to be quite healthy because they do not run deficits and do not borrow excessively. However, unlike provincial and federal governments, cities are prohibited from running deficits, and the amount municipalities are allowed to borrow is limited by provincial governments.

Experts agree that "the required balance has been achieved in large part by under-investing in infrastructure and service delivery."[25]

> "Expenditures up; transfers down; and hard-to-increase own-source revenues: it sounds like a prescription for a fiscal crisis. It is thus not surprising that there has been much concern with the fiscal sustainability of cities in Canada in recent years."[26]
>
> "The only way [municipalities have] to achieve a balance between revenues and expenditures, however, is by reducing expenditures or by raising property taxes. Neither prospect bodes well for meeting the economic and social challenges… facing large cities and city regions."[27]

Studies reaffirm the conclusions and recommendations brought forward in the City of Ottawa's first LRFP:

1. Ontario municipalities should not be funding income redistribution programs from the property tax base.

   "Ontario clearly needs to rethink its assignment decisions. Social services are cost-shared between the provincial and municipal governments in Ontario. Either these costs should be uploaded to the provincial government or new revenue-raising tools should be downloaded to the municipalities."[28]

   "Shifting funding responsibilities for all social service, social housing, and land ambulance expenditures to the provincial government in Ontario, as is the practice elsewhere in Canada, would not only assist local governments, it would make sound economic sense – all income distributional services should be the responsibility of the more senior levels of government."[29]

2. Cities need the autonomy to make decisions that will help them be more financially sustainable.

   "Cities can and should do more to help themselves. To do so, however, in the Canadian context they need first to be freed from the many inappropriate provincial constraints…which are currently preventing them from financing their

[25] Slack, Enid. "Fiscal Imbalance: The Case for Cities." June 1, 2006.
[26] Slack, Enid and Bird, Richard M. "Cities in Canadian Federalism." Presentation. Conference on Fiscal Relations and Fiscal Conditions. Georgia State University, Atlanta. May 2006.
[27] Slack, Enid, Bourne, Larry S. and Priston, Heath. "Large Cities Under Stress: Challenges and Opportunities." Report. External Advisory Committee on Cities and Communities. March 3, 2006.
[28] Slack, Enid and Bird, Richard M. "Cities in Canadian Federalism." Presentation. Conference on Fiscal Relations and Fiscal Conditions. Georgia State University, Atlanta. May 2006.
[29] Kitchen, Harry M. "Financing Canadian Cities In The Future?" May 21, 2004.

services adequately or efficiently, such as the presently convoluted 'capping' system… in Ontario. Cities should be able to act independently to make autonomous decisions in their areas of jurisdiction."[30]

3. Cities need new revenue streams to be successful and sustainable.

   "Some obvious ways to restore the balance between expenditure responsibilities and revenues can be suggested. These include, for example, increasing residential property taxes, user fees and borrowing, transferring responsibility for some expenditures to the provincial or federal governments ("uploading"), transferring revenue-raising power (tax room) to municipal governments (such as an income or selective sales taxes), and transferring funds from the federal and provincial governments through conditional or unconditional grants."[31]

Some progress has been made on these issues. The transfer of a portion of the federal and provincial gas tax is helping Ottawa fund its public transit needs. In addition, the Ontario government has established a Provincial-Municipal Fiscal and Service Delivery Review to try to create a sustainable provincial-municipal relationship for both orders of government.

In 2001, a KPMG study found that, between 1998 and 2000, for each additional tax dollar of revenue the City generated from economic growth, 91 cents went to the federal and provincial governments and only 9 cents remained for the City itself. The study was updated in 2006 to reflect the changes in taxation that have occurred since 2005. The results show that, while the total value of taxes generated for all levels of government increased by 43%, the City's share of total taxation remained at 9%. It is clear that the City is not sharing in the increased revenue arising from economic growth. However, when factoring in the transfer of provincial and federal tax revenues to municipalities, Ottawa's revenue share increases to 11% from 9%.

Progress remains slow and small in scale. If the municipal fiscal imbalance does not change soon, Canadian cities will not be able to continue to fund existing services and infrastructure.

*Ottawa depends on taxation*

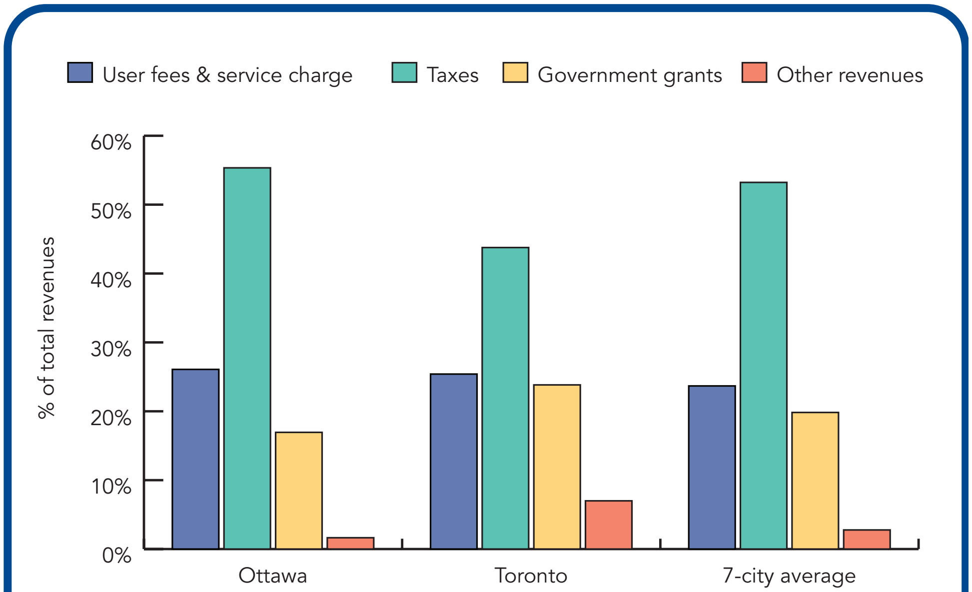
Ottawa has a higher dependence on property taxation as a source of revenue when compared to seven of the other major cities in Ontario. This is primarily due to Ottawa receiving less than its fair share of grants from other levels of government, and not being able to benefit from the pooling of social service costs like the Greater Toronto Area. In 2005, the City of Ottawa received $1.12 billion in revenue from property taxes, including federal and provincial properties that make payments-in-lieu of taxes. This represented 55.34% of the City's total revenues of $2.029 billion. Over the same period, City of Toronto taxes represented only 43.77% of total revenues. The following graph shows the reliance of the City of Ottawa on

[30] Slack, Enid and Bird, Richard M. "Cities in Canadian Federalism." Presentation. Conference on Fiscal Relations and Fiscal Conditions. Georgia State University, Atlanta. May 2006.

[31] Slack, Enid. "Fiscal Imbalance: The Case for Cities." June 1, 2006.

taxation compared to Toronto and the average of the other seven major cities or regions. Receiving a fairer share of the government grants would reduce the dependence of the City of Ottawa on taxation.

### Analysis of revenue, 2005



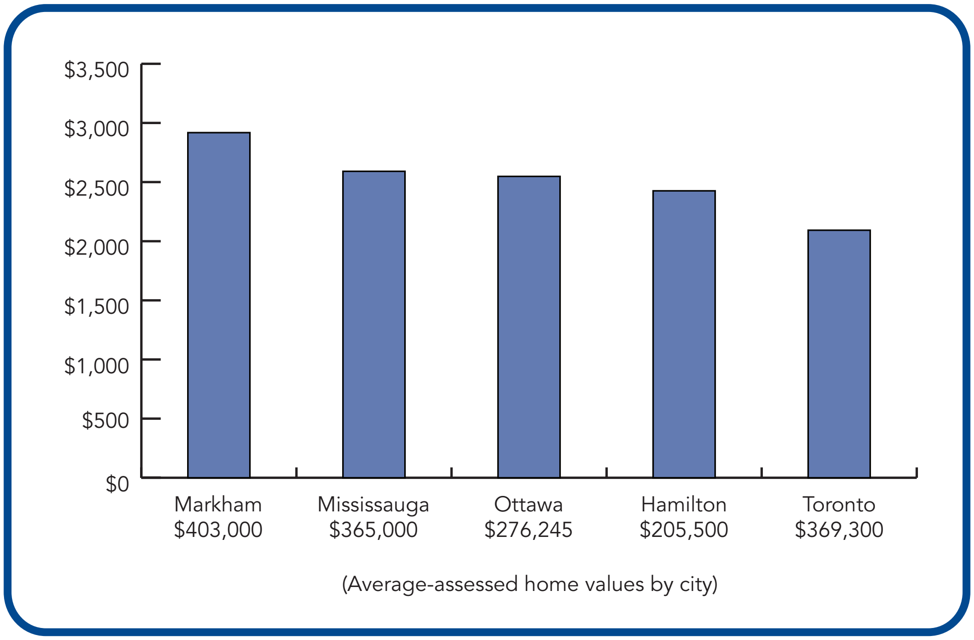

Source: 2005 FIR

*Ottawa's residential taxes are higher than in other cities*

The following graph depicts the property taxes on an average home in Ottawa assessed at $276,245 in 2006, compared to an average-assessed home in Toronto, Markham, Mississauga and Hamilton. The range in assessment value of the average home in each city reflects the variability in the cost of residential housing in each municipality. There is no common assessment value to represent what the average taxpayer pays in each municipality.

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. In 2004, the difference between the Ottawa and Toronto average municipal property tax was $515.

### Taxes paid on average-assessed home
**(Does not include education taxes)**

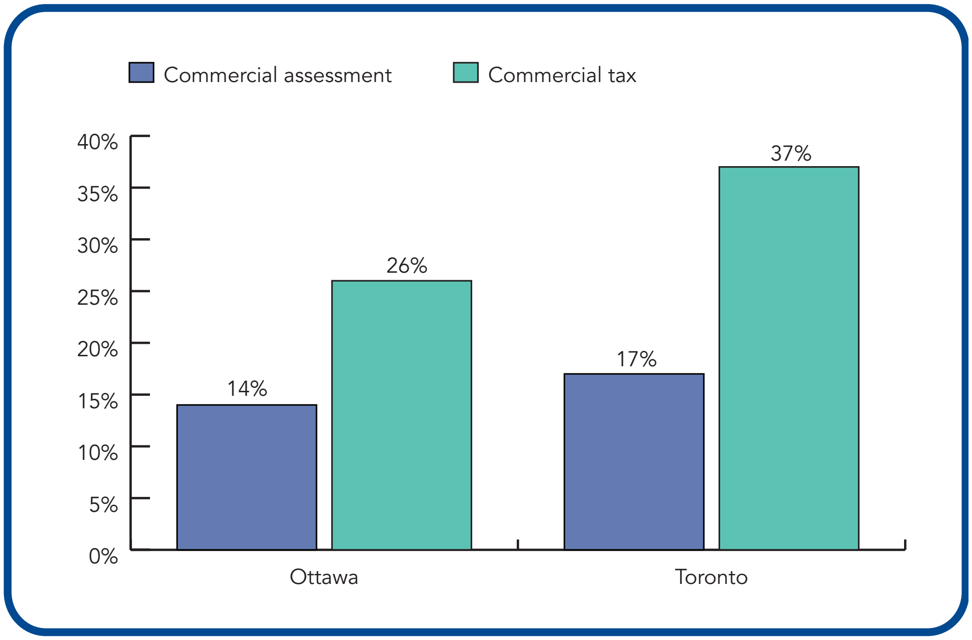



Ottawa's higher taxes cannot be explained by tax increases; Ottawa residents have enjoyed the lowest cumulative property tax increase in Ontario over the last six years. The answer lies in the difference in the relative share of commercial taxes in each city.

In Ottawa, commercial properties make up 14% of the assessment base, although these properties actually account for 26% of the tax collected. Toronto commercial properties make up 17% of the assessment base, but account for 37% of the taxes collected. Overall, commercial property owners pay proportionately more of the tax share, while residential property owners pay less. Toronto has recognized the unfair tax burden on commercial properties and is moving to reduce its commercial tax ratio. This will result in Toronto's residential taxes moving closer to those of Ottawa over time.

*The property tax system is overly complex*

**Comparison of assessment and taxation shares**




Over the last eight years, Ontario has issued many tax-related acts, bills and regulations, making the tax system very complex and challenging to understand. As a result, property taxpayers in Ontario may not be truly benefiting from the principles of fairness, equity and predictability originally intended by the Current Value Assessment (CVA) property tax system. The objective of the system was to provide a more transparent, easy-to-understand property tax model (i.e., property value multiplied by the tax rate). Instead, there are components of the property tax system that are difficult to explain to residents.

Some of Ottawa's property tax challenges include: shifts within a tax class, between classes, and between regions in the province; municipal tax restrictions on some classes; lengthy capping protection for properties in certain classes; and the impact on taxpayers required to absorb capping shortfalls. Trying to explain to taxpayers how all the changes affect their taxes has been one of the biggest challenges the City of Ottawa has faced since amalgamation. All Ontario municipalities share this challenge to varying degrees.

A brief description of the issues and their impact follows.

### Commercial taxes – capping and clawback

There has been much criticism about the differences between residential and commercial taxation in Ontario as well as the complexity of commercial property taxation. Commercial tax classes include multi-residential properties (low- and high-rise apartments and town-house units), commercial properties (retail stores, banks, offices) and industrial properties (manufacturing, warehouses). Changes to municipal property taxation introduced by the Province in 1998 required municipalities to limit, or cap, any tax increases for commercial properties.

While the intent of the capping legislation was to provide predictability for commercial taxpayers, it has led to a significant problem for smaller commercial properties that now have to pay more than they should, in some instances.

Under the current capping legislation, any assessment-related property tax increase for a commercial property is limited to the greater amount of 10% of the previous year's taxes or 5% of the real CVA taxation. Assessment-related tax increases to commercial properties are limited by the capping legislation. Individual properties protected by the cap generate a "taxation shortfall" within the tax class (i.e., all properties falling in that class). This "taxation shortfall" is the difference between the amount of CVA taxes that the properties would generate and what they generate with the capping limit applied. This tax shortfall has to be recovered from other taxpayers within the class, which results in increased tax for other commercial properties.

The mechanism to recover this tax shortfall from other properties is called a "clawback." Under this process, properties that would get a tax decrease because of a reduction in assessment have the decrease reduced, or eliminated, in order to cover the shortfall. In other words, commercial taxpayers who would be entitled to a reduction in their taxes because of a reduced assessment pay additional taxes to make up for taxes not paid by other commercial taxpayers because of the capping limit.

The following table shows that, in 2005, the City of Ottawa had a taxation shortfall of $22.8 million because of capping, which was recovered primarily from smaller commercial properties that would otherwise have experienced a reduction in property tax.

| **Annual taxes ($)** | **Clawback (More than CVA)** | | **No adjust-ment (At full CVA)** | **Capped (Less than CVA)** | | **Result** |
|---|---|---|---|---|---|---|
| | # Accounts | Total Clawback ($) | # Accounts | # Accounts | Total Capped ($) | Net Benefit |
| 0 – 200,000 | 4,014 | 15,696,669 | 3,183 | 1,853 | 5,356,322 | (10,340,347) |
| 200,000 – 500,000 | 112 | 3,550,131 | 48 | 52 | 2,680,749 | (869,382) |
| 500,000 – 1,000,000 | 7 | 1,042,781 | 2 | 4 | 2,273,315 | 1,230,534 |
| 1,000,000 – 1,500,000 | 9 | 471,815 | 8 | 6 | 630,781 | 158,966 |
| 1,500,000 – 2,000,000 | 1 | 219,993 | 1 | 3 | 351,000 | 131,007 |
| 2,000,000 – 3,000,000 | 1 | 280,008 | 1 | 4 | 1,297,170 | 1,017,162 |
| 3,000,000 – 5,000,000 | 1 | 384,034 | 2 | 7 | 5,293,268 | 4,909,234 |
| 5,000,000 – 10,000,000 | 3 | 1,180,140 | 0 | 6 | 4,943,866 | 3,763,726 |
| Total | 4,148 | 22,825,571 | 3,245 | 1,935 | 22,825,571 | |

The table also shows that the beneficiaries of the capping program are primarily commercial properties with higher assessed values.

The Province also established "the provincial threshold" for tax ratios. These thresholds were established in 1998 based on assessment values at that time. This was intended to prevent municipalities from applying any budget-related tax increases to commercial properties if the tax ratio is was higher than the threshold.

Ottawa was below the threshold until 2004. Since then, as a result of adopting tax ratios that prevent tax shifts between classes, the commercial ratio has risen above the threshold. Therefore, the City of Ottawa has only been able to impose a budgetary tax increase for commercial properties at half the rate of the residential increase for the last two years. Consequently, the other tax classes have had to absorb a greater share of the budgetary tax increase, with residential (the largest class) absorbing the biggest share.

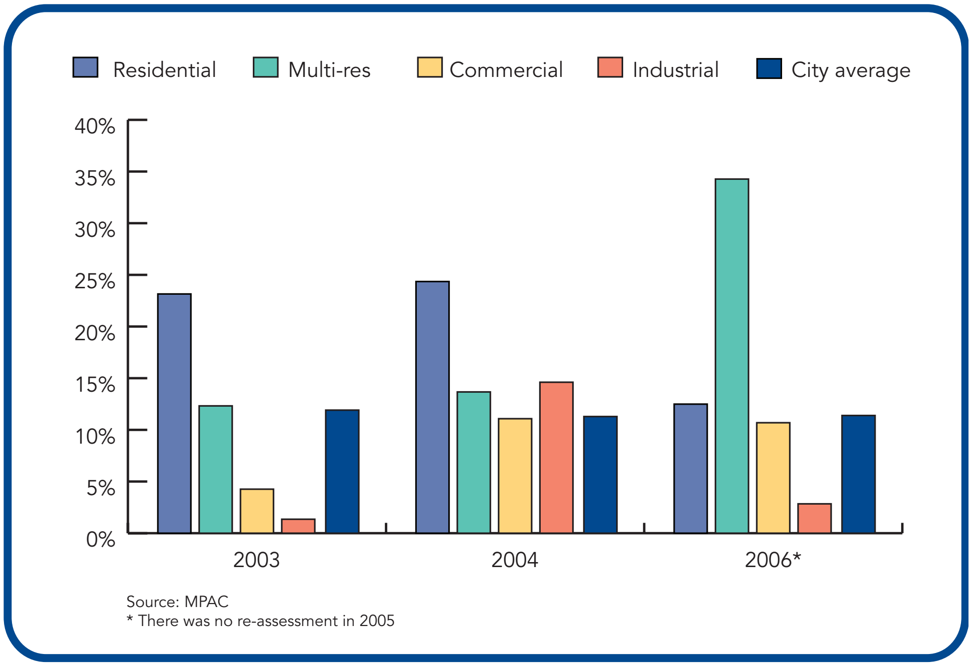
The Province's tax policy was meant to move all properties to their full CVA. Under the capping program, there is no time limit as to when properties should be at their full CVA taxation (CVA assessment multiplied by tax rate). In each year where there is a re-assessment, progress towards full CVA taxation is disrupted because the new assessment values have to be incorporated into the scenario. The current two-year freeze in assessments recently announced by the Minister of Finance will provide some progress towards full CVA, but will not solve this problem in the longer term.

Capping was intended to move the current taxation system towards one based on CVA within a reasonable timeframe. Instead, it has perpetuated tax inequity within the commercial classes, where taxpayers entitled to lower taxes based on their full CVA taxes are denied their full reduction in order to subsidize properties with large CVA increases. Annual re-assessments were intended to alleviate large, unpredictable one-time increases of several years of incremental property values. Instead, the inequity of the capping program continues.

### Residential taxation – tax shifting from other classes

In contrast to commercial taxation, for residential property taxation there are no tools in place, like capping, to reduce the impact of assessment changes. The last three assessment increases for residential and multi-residential properties have been higher than for commercial properties over the same period. The following graph shows the average increase in each class compared to the average increase across all classes for the last three re-assessments. Note that when the total assessment for a class rises above the city average, properties in the class above the average pay more tax while those below pay less.

## Average assessment change in each tax year, by class

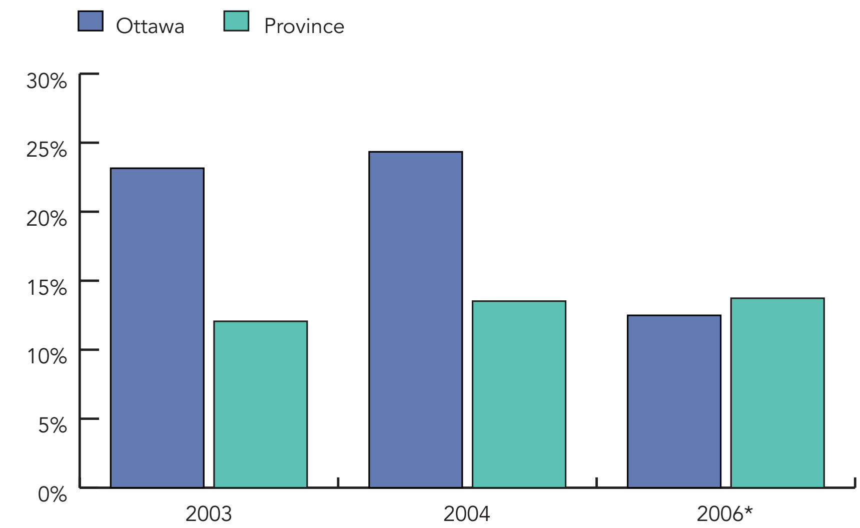



This situation first occurred unexpectedly in 2003 when there was a tax burden shift from the commercial property class to the residential class. At that time, there were no taxation policy tools available to Council to eliminate the impact of the shift. Furthermore, Ottawa was almost alone in Ontario in experiencing this type of shift and was forced to appeal to the Ontario government for mitigation tools. For 2004 and 2006, the Province temporarily allowed municipal councils to eliminate the tax shift through the use of "neutral tax ratios." A neutral tax ratio gives a heavier weight to assessment of the tax class that is losing tax so that the burden does not shift.

*Residential taxes – shifting of education taxes*

The last three re-assessments also created significant differences between the changes in assessment values of Ottawa residential properties and those of other Ontario municipalities. Ottawa's strong residential housing market resulted in larger average increases in assessment value than the provincial average. The following graph shows the magnitude of the differences in assessment for Ottawa as compared to the rest of the Province.

## Change in average residential assessment



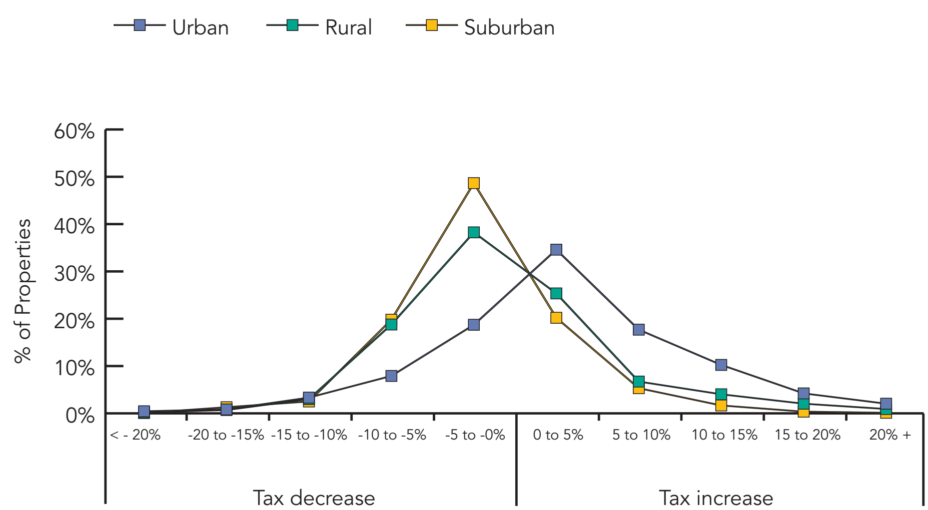

Source: MPAC
* There was no re-assessment in 2005

The Province sets residential education tax rates using assessment values from all Ontario municipalities. Given that Ottawa residential assessment values have risen higher than the provincial average, the education tax burden has shifted from other areas of the province to Ottawa. From 2001 to 2005, the City's assessment base grew 11.1% from the addition of new properties. Over the same period, education taxes increased for residential properties by 33.7%. This has cost Ottawa residential taxpayers $28 million more than taxpayers in other Ontario municipalities.

*Residential taxes – inability to phase in increases*

In each re-assessment, there has been significant tax shifting within the residential class as properties in some areas of the city experience much greater increases in value than others. The following graph shows the percentage of properties in urban, suburban and rural areas of Ottawa, as well as how much their taxes changed as a result of the last assessment. Generally, assessment values in the suburban and rural areas of the city are increasing at a lower rate than in the urban areas. This has been true in each of the re-assessment years. Unlike the commercial classes, the residential class phase-in is not mandatory and would be practically impossible to implement with annual re-assessments.

## Tax impact of 2006 re-assessment: residential properties




Source: City of Ottawa

### Multi-residential taxes

Rental rates for apartments in Ottawa continue to increase. A portion of these rent payments contributes to property tax. City Council has always indicated a preference for a fair level of taxation between multi-residential and residential properties. The difficulty in making the comparison between the two types of properties is that the Province has determined that residential properties be valued on the sales approach (based on market sales) whereas multi-residential properties are valued on the income approach (based on cash flow from rent payments). There is no existing agreed-upon methodology for comparing the tax burden between residential and multi-residential properties.

As a result, Council has been making incremental changes in the taxation burden of the multi-residential class. Since 2001, the burden for this class has been reduced by more than $3 million, in spite of tax shifts into the class and tax levy increases. In 2000, the multi-residential class represented 6.14% of the assessment base and 11.6% of all City taxation. Today, the multi-residential class represents 6.6% of the assessment base but only 9.6% of the total tax bill. The result is that Ottawa's taxes per suite for a walk-up apartment in 2005 were $177 and $163 less, respectively, for mid- and high-rise apartments than the average for municipalities with populations greater than 100,000.[32] In 2006, Council reached the 2004 tax ratio target they had set for the multi-residential tax class.

[32] BMA Management Consulting, "Municipal Study," 2005, p. 127.

*Farm taxes are among the lowest*

Since amalgamation, City Council has reduced the farmland tax ratio significantly to recognize the importance of the farm sector to the City of Ottawa. In 2005, of 47 municipalities in Ontario with the farmland tax class, the City of Ottawa levied the second lowest taxes per acre – 84% lower than the provincial average taxes per acre for Class 1 farmland, and 73% lower than the provincial average taxes per acre for Class 6 farmland.[33]

With fuel costs rising and financial pressures increasing for the farm community, City Council introduced a Farm Grant Program in 2006. This allows farmers to defer the final payment of their 2006 tax instalment until after they have harvested their crops.

### Tax mitigation tools needed

The public holds municipalities accountable for their property tax bill; therefore, municipal councils need more control over the tax and assessment systems. The types of policy tools municipal councils should have at their disposal include:

- Mitigation tools to counter the effects of large assessment increases and associated tax shifts experienced by a class during a given cycle;
- Flexibility to accelerate movement towards full CVA taxation for the classes that are currently capped;
- The ability to implement a phase-in program for residential property owners by adopting a re-assessment only every three to five years; and
- The ability to set education taxes based on a levy requirement identified by the Province.

Over the years, staff and Council have provided suggestions to the Province on how to improve the municipal taxation system in Ontario. The Province has shown support for Ottawa by implementing requests for mitigation tools but the dialogue must continue to fix the property tax system.

## USER FEES AND CHARGES

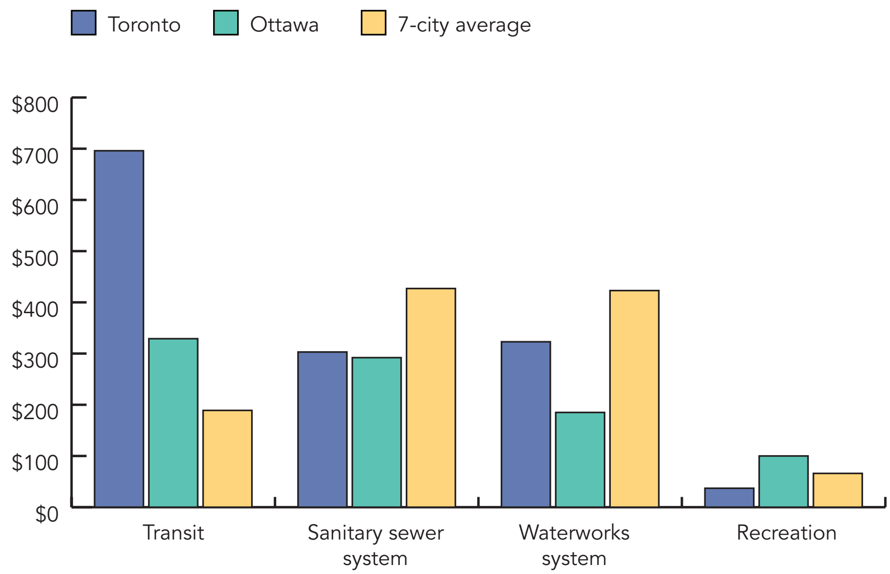
Under the *Municipal Act*, municipalities have broad authority to impose fees or charges for any activity or service they provide. While municipalities can determine which services to charge for, the amount of the fee and who pays it, the *Municipal Act* limits them to cost recovery – in other words, municipalities cannot charge more than it costs them to provide a service.

The main user fees in Ottawa are transit fares, water rates, sewer surcharge, and registration and entry fees for recreation programs and facilities. User fees and charges directly fund a portion of the program or service costs. Since 2004, user fees have increased annually as the City strives to maintain a constant cost-to-user fee ratio. In 2005, the City collected $484 million in user fees and charges. By passing all or a portion of cost increases on to users, the City can take pressure off the residential property tax bill.

[33] BMA Management Consulting, "Municipal Study," 2005, p. 172.

A comparison of user fees on a per capita basis is provided in the graph below.

### Comparison of user fees and charges, per household




Source: FIR

With the second largest transit ridership levels in the province, Ottawa collected approximately $115 million in transit fares in 2005, covering 37.5% of total transit expenditures, including contributions to capital. The 2005 Ontario municipal average for transit revenues as a percentage of expenditures was 42.9%. Last year, Council adopted a policy to recover 55% of direct transit expenditures from the users, thus bringing Ottawa closer to the provincial average and covering increasing expenditures. Ottawa is not unique. All Ontario municipalities have had to increase their transit user fees due to economic factors, such as higher gas prices.[34]

In 2005, water rates and sewer surcharges totalled $64 million and $102 million, respectively. For an average household, this amounted to $645 per year, up $53 from the previous year. The average municipal cost in Ontario for water and sewer services in 2005 was $665, up 19% from 2004. The City of Ottawa and most other municipalities across Ontario have increased user fees for water and sewer services to protect public safety, ensure infrastructure reliability and meet provincial obligations.

[34] BMA Management Consulting Inc., "Municipal Study," 2005, pp 73-74.

User fees for recreational services totalled $35 million in 2005, representing 35% of total expenditures for the service.[35] While taxes still cover 65% of the cost of recreational services, Ottawa collects more user fees for this category than Toronto and the seven-city average on a per capita basis: $100 per household for recreational fees compared to $66 for the Ontario seven-city average and $37 for Toronto. The City has ensured that low-income families are not priced out of recreational programs by increasing the amount of subsidy by an amount equivalent to any user fee increase.

In implementing the user-pay principle, the City has also moved garbage collection from the assessment-based tax bill to a flat user fee for both residential and multi-residential properties. The user fee for garbage collection is part of a larger strategy to increase awareness of the cost of garbage and ultimately increase recycling rates. By removing this cost from the property tax system, commercial and industrial properties that do not receive the service from the City no longer have to pay for it.

### New user fees and charges

In 2005, the City identified a number of revenue opportunities, including new user fees, for the Province to consider as part of the new *City of Ottawa Act*. The City was not given any of these revenue options, but the Province indicated it would study them further in its review of the *Municipal Act*. At the time of this report, Bill 130, the *Municipal Statute Law Amendment Act*, has already undergone first reading. However, the amendments to Bill 130 do not include any new financial tools.

### Funding from other levels of government has declined

As discussed previously, the City receives funding from the provincial and federal governments, mostly for cost-shared social programs. Since the early 1990s, successive federal and provincial governments have balanced their budgets by downloading services or reducing funding support to municipalities. Several grant programs slowly disappeared during the 1990s, including transit and road services grants, and unconditional grants that provided general funding to help municipalities reduce the cost of providing local services.

In 1998, the Province introduced a provincial-municipal service realignment, which was promoted as "revenue neutral." The Province harmonized education tax rates during the same period and introduced a province-wide education tax rate, which resulted in lower education costs on residential tax bills. However, more services and costs were downloaded to municipalities during that exercise to be added to the municipal portion of the tax bill. Over the years, governments have further reduced the level of funding for these downloaded services.

[35] FIR 2005.

For example, in 1997, provincial grants covered 77% of Ottawa's total social assistance spending. By 2005, these grants were reduced to 54% of the total costs. In 2001, provincial grants funded almost 31% of total social housing expenditures. By 2005, this had decreased to 24%.[36]

As a result of the changes to social housing grants, the waiting list for subsidized housing in Ottawa has increased dramatically and the City does not have the funding to handle the extra demand. As of December 31, 2005, 9,922 applicant households were wait-listed, meaning that about 23,000 Ottawa residents face an average waiting period of five to eight years for subsidized housing.

Increased service responsibilities, coupled with reduced funding, have presented municipal councils with challenges in balancing community needs with maintaining reasonable levels of taxation. In many cases, maintenance of city infrastructure has been deferred to achieve a balance between these competing objectives.

The good news is that, starting in the late 1990s, a number of federal and provincial programs were launched to address capital infrastructure requirements. These programs help municipalities fund critical infrastructure and meet community infrastructure growth needs. Programs such as the Canada-Ontario Infrastructure Works program (COIW), Transit Investment Partnership (TIP) and SuperBuild have greatly assisted municipalities in addressing deficiencies in their road, transit, sewer and water systems.

However, although well intentioned, these programs are short-term and require renewal. Many of them restrict how funds are to be used and, most importantly, do not provide base funding on which municipalities can rely each year. In addition, as governments change, so do priorities and funding commitments. Consequently, such programs cannot be considered sustainable and predictable sources of funding that allow municipalities to properly plan and manage their capital and operating responsibilities.

In response to the Province's 2006 spring budget, the Association of Municipalities of Ontario (AMO) President, Roger Anderson, stated: "One-time funding announcements help with the symptoms of downloading – but they do not protect the municipal property taxpayer from the ongoing burden of downloaded provincial costs." Although this type of funding benefits municipalities, it fails to address the urgent need to restore fiscal sustainability to municipal governments in Ontario.

[36] FIR 1997, Regional Municipality of Ottawa-Carleton, 2001 Ottawa, 2005 Ottawa.

## OTHER SOURCES OF REVENUE

While expenditures tend to increase year over year across all categories, the same is not true for revenues. The City must look beyond taxation and user fees to other sources of revenue, such as interest earnings and dividends, to help fund its programs. However, Council does not control the direction of interest rates and dividends. The City of Ottawa also generates revenue from dividend payments from Hydro Ottawa and the Rideau Carleton Raceway. Other sources of revenue constituted 1.64% of the total revenue in 2005; without these other revenue sources, taxes would have increased $33 million or 3.5%.

### Interest earnings

The City's main non-tax or user fee revenue comes from interest on funds not immediately required for use. *Municipal Act* regulations establish the investments the City can undertake, which tend to be a relatively conservative mix.

While the types of investments the City can make are limited, it is still important to maximize returns through benchmarking with other municipalities. Benchmarks include:

- ONE Fund – municipal pooled investment program designed specifically for the Ontario public sector, overseen by the CHUMS Financing Corporation and Local Authority Services Limited.
- Scotia Capital Three-Month Treasury Bill Index – composed of three-month Canada treasury bills, which are rolled into new bills at each Government of Canada Treasury bill auction.
- A composite of the Scotia Capital All Governments Short-Term and Mid-Term Bond Indices – consists of federal, provincial and municipal bonds with remaining effective terms greater than one year and less than or equal to 10 years.

While none of these benchmarks precisely reflects the investment policy, or the City's goals and objectives, they serve as a reasonably acceptable basis for comparison. The table below compares City and benchmark returns.

#### Comparison of investment performance

| | Returns (%) | | | | |
|---|---|---|---|---|---|
| | 2001[37] | 2002 | 2003 | 2004[38] | 2005 |
| City – All funds[39] | 4.77 | 4.22 | 4.24 | 4.34 | 3.45 |
| Scotia Capital Indices (SCI)[40] | N/A | 4.09 | 3.63 | 4.26 | 3.17 |
| ONE Fund[41] | 4.38 | 3.63 | 3.61 | 3.66 | 2.27 |
| City exceeds SCI | N/A | 0.13 | 0.61 | 0.08 | 0.28 |
| City exceeds ONE Fund | 0.39 | 0.59 | 0.63 | 0.68 | 1.18 |

[37] For 2001, only Money Market returns are shown.
[38] As of 2004, City returns are shown on a total market return basis.
[39] City returns are shown on a book basis prior to 2004.
[40] SCI portfolio management fees and expenses have not been deducted.
[41] ONE Fund returns are shown after incurring investment management expenses.

The current legal framework within Canada limits municipalities' ability to manage and regulate the programs and services they deliver. In the United States and Europe, considerable effort has been made to allow cities to determine which services to provide and how to fund them.

## *Comparison with other jurisdictions*

In recent years, provincial governments across Canada have provided municipalities with additional authority to raise new revenues or have transferred to them portions of their income or gas tax revenues. Although the Province of Ontario has made headway in providing municipalities with a portion of their gas taxes, it must make additional funding sources available to restore municipal fiscal sustainability.

The following table compares the municipal revenue sources in the United States and Canada.

### Municipal fiscal authority: Canada and the U.S.A

| | U.S.A. | BC | Alberta | Manitoba | Quebec | Nova Scotia | Ontario | Other provinces & territories |
|---|---|---|---|---|---|---|---|---|
| Property tax | x | x | x | x | x | x | x | x |
| Sales tax | x | x | | | | | | |
| Hotel/motel tax | x | x | | | x | | | |
| Business tax | x | x | x | | x | | | |
| Fuel tax | x | x | x | x | x | | x | |
| License fees | x | | | | | | | |
| Income tax: individual and corporate | x | | | x* | | | | |
| Development charges | x | x | x | | | | x | |
| Tax-exempt municipal bonds | x | | | | | | x | |
| Tax incentives | x | | | | | | | |
| Grants to corporations | x | | | | | | | |
| Borrow money | x | x | x | x | x | x | x | x |

*Note: Available to Winnipeg
Source: Federation of Canadian Municipalities

# PART C: CAPITAL ASSETS

## VALUATION OF CAPITAL ASSETS

As presented in the table below, the City's major types of infrastructure have an approximate replacement value of $26.4 billion. These assets include roads, water and sewer networks, public transit, buildings, buses and paramedic vehicles. Buildings are further broken down by facility type in the second table. In general, Ottawa's capital assets in the downtown core are older than in suburban areas. A complete valuation of assets is underway to address the Public Sector Accounting Board's (PSAB) requirements. These are discussed further in this section.

### Estimated replacement value of Ottawa's capital assets

| Type of infrastructure | Composition | Estimated replacement value |
|---|---|---|
| Transportation infrastructure | 5,397 km of roadways<br>569 bridges and structures<br>1,580 km of sidewalks | $10,486,620,000 |
| Environmental infrastructure | 69 waste water pump stations<br>1 waste water treatment plant<br>2,430 km of sanitary sewer networks<br>2,150 km of storm sewer networks<br>11 storm water pump stations<br>152 storm water devices / facilities<br>2,730 km of piped water distribution<br>2 water purification plants | $12,268,450,000 |
| Public transit system | 10 Park and Ride facilities<br>19 Transitway stations | $720,820,000 |
| Buildings and facilities | 783 structures including recreational facilities, fire halls, police stations, libraries, ambulance buildings, etc. | $2,051,757,146 |
| Fleet | 84 paramedic vehicles<br>107 fire trucks<br>692 heavy fleet<br>1,320 light fleet and equipment<br>942 transit buses | $768,063,000 |
| Information technology | 7,084 desktop computers and applications<br>1,622 printers<br>812 laptops<br>440 business applications | $82,131,000 |
| **Total** | | **$26,377,841,146** |

Source: City of Ottawa

### City-owned buildings, by facility group

**(Active status with area greater than 100 sq. ft.)**

| Facility group | Quantity | Total area (sq. ft.) | Average age (yrs) | Effective replacement value |
|---|---|---|---|---|
| Recreation | 267 | 3,380,399 | 35 | $628,200,094 |
| Public Works | 149 | 3,145,437 | 24 | $452,255,399 |
| General Purpose | 162 | 933,561 | 35 | $234,246,919 |
| Transit Services | 32 | 1,036,941 | 18 | $199,260,700 |
| Civic Administration | 18 | 1,303,070 | 35 | $178,756,026 |
| Protective Services | 60 | 893,570 | 22 | $172,401,743 |
| Arts and Culture | 76 | 481,215 | 67 | $98,213,165 |
| Social Services | 19 | 610,698 | 30 | $88,423,100 |
| **Total** | **783** | **11,784,891** | **33** | **$2,051,757,146** |

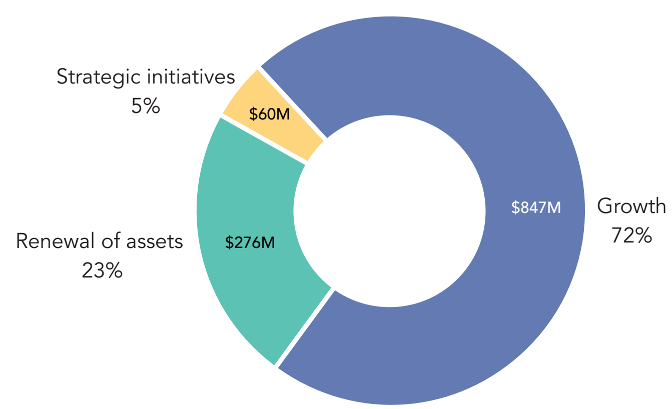
Source: City of Ottawa

## CAPITAL EXPENDITURE OVERVIEW

A capital expenditure is defined as any significant expenditure incurred to acquire or improve land, buildings, engineering structures, machinery and equipment that confers a benefit lasting more than one year and results in the acquisition or extension of the life of a fixed asset. In 2006, Council approved $1.183 million in new capital expenditure, comprising $847 million for growth projects, $276 million for asset renewal and $60 million for strategic initiatives.

### 2006 capital budget expenditures, by category

**($1,183 million)**




Source: City of Ottawa

## Categories of capital works

**Renewal of City assets** – This category covers the funding required to maintain or replace all existing capital assets throughout the full life of the assets. These assets include buildings, structures, roadways, transitways, bridges, vehicles, equipment, computers, computer networks and various other facilities.

Studies have been undertaken throughout the various City program areas to determine what funding is required to maintain the asset at provincial or federal standard levels. Reports have been brought to Council over the past two years that recommend related lifecycle maintenance projects. Capital priorities, identified as renewal projects within the capital budget, are based on those studies. The goal is to fully fund identified lifecycle needs within a 10-year period.

**Growth** – This category includes all projects identified in the Development Charges Background Study and priorities contained in the 2004 Official Plan. Funding from this source reflects the most recent changes to the Development Charges By-law, approved by Council on December 8, 2004. Additional information on this by-law is provided later in this section.

**Strategic initiatives** – This category includes all other capital expenditures, such as: the implementation of various master plans or the Ottawa 20/20 plan; acquisition of environmental areas; enhancement of current services and growth costs not funded through development charges. It also includes initiatives to enhance organizational effectiveness, new legislated requirements, Council-approved programs not related to growth, and changes in demand for services.

## Capital assets will be added to the City's balance sheet

One of the more significant changes introduced by the PSAB is a shift to full accrual accounting for tangible capital assets, such as roads, buildings, land, water systems, office furniture and vehicles. This is a significant accounting change and means Ottawa will add tangible capital assets to its financial statements in 2009. Assets will be expensed in the same time period in which they are consumed. For example, if a road costs $20 million to build and is expected to last for 20 years, a $1-million expense will be recorded each year as the value of the asset used in the year.

This reporting change will take significant resources to plan and implement – the City is currently in the planning stages of this project. An inventory will be undertaken of all assets, including each asset's value, useful life and depreciated value.

Adding tangible capital assets to financial statements will provide better information to decision-makers as they plan for related maintenance and replacement costs. It will also give residents clear information about spending on capital assets. The PSAB aims to reinforce municipal stewardship responsibilities and provide information to hold municipalities accountable for capital spending decisions.

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."

The inclusion of tangible capital assets on financial statements is a step towards making this deficiency transparent to Council and residents.

### Operating impacts from capital construction

Each year, the City builds new infrastructure (roads, traffic lights, community centres) or purchases assets (buses, fire trucks) to address community growth requirements. The City also receives what is termed as "donated assets," such as residential roads or water and sewer mains from developers once new communities are built. Since receipt of these assets does not involve municipal capital expenses, they are not included in the City's capital budget.

However, once assets are built or received, they must be maintained and repaired on a regular basis. They also require City staff to operate them to provide service to the public. Ongoing operational costs associated with building or receiving assets have a significant impact on the City's operating budget.

In 2006, approximately $7.5 million was added to the City's operating budget to address these types of growth-related costs, representing a tax increase of 0.8%.

The following table provides some examples of where the City's capital program has a monetary and/or personnel impact on the operating budget:

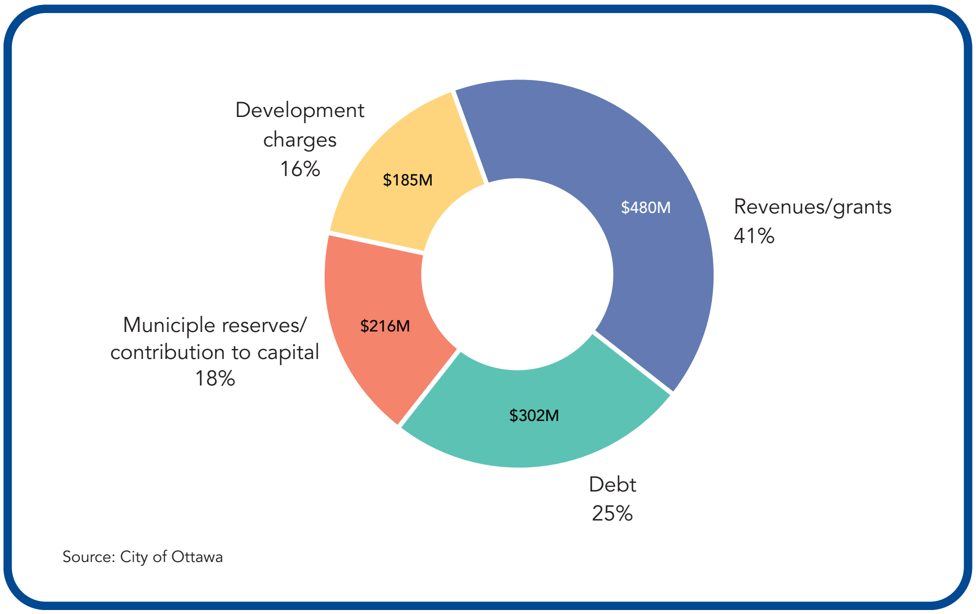
| City service | Impact |
|---|---|
| Real Property Asset Management | Costs including hydro, water and maintenance and repairs for new facilities like fire stations, libraries, community centres, sportsplexes, field houses |
| Information Technology | Computers and peripherals maintenance costs for the additional growth-related staff |
| Paramedic Services | Ambulance fleet costs (e.g., fuel) |
| Fire Services | Maintenance costs for fire vehicles; staff for new fire stations |
| Parks and Recreation | Hydro and water costs related to the opening of new parks |
| Library | Staffing costs for new facilities |
| Surface Operations | Repair costs and snow clearing of additional lane kilometres of roadways and sidewalks; maintenance costs of additional hectares of sports fields |
| Traffic & Parking | Hydro costs for new traffic signals and street lights |
| Transit | Fuel and parts for new buses |
| Drinking Water Services | Maintenance costs for additional kilometres of watermains (including valves, hydrants); operating costs related to expanded treatment plants |
| Wastewater Services | Maintenance costs for additional kilometres of trunk sewers; costs for additional stormwater facilities |

## CAPITAL FUNDING OVERVIEW

Municipalities finance capital costs through reserves and reserve funds, provincial and federal grants, contributions from developers and long-term borrowing. The graph below depicts the 2006 capital budget broken into four financing categories: revenues and grants, reserves, development charges and debt.

### 2006 capital budget financing

**($1,183 million)**



## Funding principles

The two previous Long-Range Financial Plans identified a number of funding principles for the City to use in developing the capital budget. These principles include:

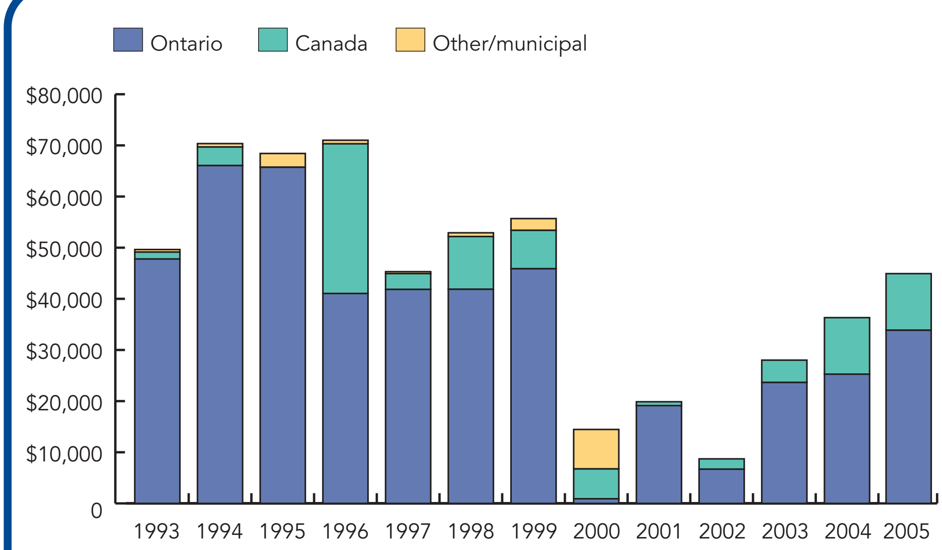
- Maintain the current tax-supported debt servicing costs by allowing approximately $40 million in new tax-supported debt authority each year (not including Police Services).
- Maintain the tax-supported reserve balances at $50 million and the rate-supported reserves at $20 million.
- Finance the City portion of the expansion of rapid transit and other growth-related projects through debt financing and apply future gas tax payments to pay the debt charge.

In addition, Council adopted the policy of increasing annual contributions to capital reserves based on the City's Infrastructure Construction Price Index as published by Statistics Canada.

## Revenues and grants

At $480 million, revenues and grants represented the largest portion of capital financing in 2005. However, federal and provincial capital grants have decreased significantly from the early 1990s, as shown in the graph below, putting more pressure on the City to find other sources of financing.

### Capital grants, 1993-2005
**($ thousands)**




Source: City of Ottawa

## Federal and provincial gas tax

Over the past few years, both the federal and provincial governments have reinvested in municipal infrastructure by sharing gas tax revenues.

The provincial government has committed to permanently providing two cents of its gas tax to municipalities. The revenue is to fund transit capital initiatives that increase ridership or pay for operating costs. The City's share of the provincial gas tax will peak at $37.3 million in 2007. Of this amount, Council determined that $7.1 million is to fund growth-related operating costs. Council approved the remaining $30.2 million to service debt used to fund the Light Rail Transit project.

Municipal revenues from the federal gas tax will increase to a peak of $50 million per year by 2009. Federal gas tax revenues must be spent on transit capital projects; however, the federal government has stipulated that this funding cannot be applied to the Light Rail Transit Project. In addition, Bill C-66 will provide municipalities with additional federal gas tax revenues totalling $40 million in 2006 and 2007.

## Development charges

The amalgamated City of Ottawa established its first Development Charges (DCs) by-law in July 2004. DCs are paid when developers build new communities and are designed to pay for capital facilities that service growth such as new roads, sewers and watermains. These charges do not fund replacement, rehabilitation or City operating costs.

Council policy is that growth should pay for itself. Provincial legislation directs that revenue recovered from development charges must not exceed actual costs. The *Development Charge Act* was amended in 1997, and as a result, DCs no longer cover growth costs such as:

- Service discounts: Municipalities are required to finance 10% of the growth-related costs of providing transit, parks, recreation, child-care, libraries, paramedics, studies, work yards and vehicles. As a result, 10% of these growth-related costs are excluded from the DC and must be financed through taxes or existing user fees.
- Service levels: The DC is calculated to recover costs based on the average level of service over the previous 10 years. If Council wants to provide a level of service beyond the 10-year average, it will not be covered by DCs and must be financed through taxes or user fees.
- Excluded services: Amendments to the Act in 1997 excluded charges for park-land acquisition, cultural facilities and solid waste. As a result, all capital projects in these areas are funded from non-DC sources.

- Excess capacity: To ensure minimum disruption and cost, municipalities often build oversized sewers and watermains to meet future growth needs. However, provisions of the Act make it difficult to use current growth to pay for that portion of the capital works that may benefit future growth.

These are just a few areas in the legislation that need to be addressed to make growth truly pay for itself.

### Other revenue sources

In addition to the sources of revenue already cited, the City has a number of non-tax sources to fund capital requirements, including:

- Cash-in-lieu of parkland, a requirement of the *Planning Act* that is paid by developers if they do not provide the required amount of green space in a new development
- Cash-in-lieu of parking, a requirement of the *Planning Act* that is paid by commercial property owners if they cannot provide the required number of parking spaces for their property

### Debt financing

The first Long-Range Financial Plan contained the following recommendation in an effort to confine debt financing to certain types of projects:

> "Long-term debt financing should be restricted to specific project types. Debt funding for lifecycle projects should be reduced and ultimately eliminated. Instead, debt financing should be employed on projects related to capacity expansion or growth, projects financed by development charges, future new non-traditional infrastructure projects, and projects tied to third-party matching funding. These restrictions may have to be phased in to meet short-term budget challenges."

The rationale for the use of debt as a financing mechanism is that it spreads the cost of major growth projects over a number of years, similar to a mortgage on a home. Consequently, such projects are paid for by a broader tax base, making the forecast in the 10-year capital work plan achievable.

Repayment of principal and interest charges is funded from property taxes, revenue derived from water and sewer surcharge rates, or from non-tax/rate-supported revenues such as federal and provincial gas tax revenues and DCs. Additional debt will be issued from non-tax/rate-supported sources over the next four years, as discussed earlier in the section on Council-controlled programs.

# OPERATING FORECAST – TAX-SUPPORTED PROGRAMS AND SERVICES

The Long-Range Financial Plans I and II focused on identifying capital infrastructure requirements for the newly amalgamated City of Ottawa and examined available funding sources. Strategies and recommendations were provided and implemented to assist Council in addressing significant funding "gaps" identified in those reports.

LRFP III includes a 10-year forecast of capital requirements and associated strategies to address revisions to the funding gaps. It also contains a four-year term-of-Council operating forecast that provides Council and residents with a long-term, integrated, picture of the City's financial pressures, which is based on the best information currently available. The operating forecast represents cost and revenue projections for property tax-supported programs and services. Cost and revenue projections for rate-supported programs, like water and sewer services, are discussed in a separate section.

### *2007-2010 operating forecasts versus 2007-2010 draft budget estimates*

The Ottawa Police Service 2007 operating forecast, as identified in the 2006 budget process, has been adjusted by Police Service staff and has been included in the overall forecast. Police Service staff have also provided a high-level forecast for 2008 to 2010. A separate detailed Police Service LRFP report will be produced and tabled with the Ottawa Police Services Board.

The 2007-2010 forecast for tax-supported programs provides Council and residents with a high-level overview of estimated expenditures and anticipated revenues over the next four years, based on the best available information at this time. These estimates will be further refined and adjusted during the upcoming weeks as departments develop their draft budget requirements. These changes along with Council's direction to staff through the companion report — 2007 Budget Directions — will be incorporated into the draft budget estimates to be tabled in February 2007.

The 2008 to 2010 forecasts will be tabled with Council for information, rather than approval. These forecasts will form the basis for subsequent annual budget cycles.

## BUDGET PRESSURE CATEGORIES

Every year, the City faces a number of cost pressures that must be addressed to set the budget and to finalize taxes for the year. The budget pressures facing the City in the near- and medium-term have been categorized as follows:

**Maintain existing services –** additional funding requirements to continue delivering City programs and services at current Council-approved service levels. Increases in compensation resulting from collective agreement settlements are the largest cost in this category. Inflationary increases in energy costs, contracted services, materials and supplies are also included in this category.

In 2005 and 2006, $50 million and $60 million respectively were added to the budget to cover the costs of maintaining services. Increases in user fees have partially offset some cost increases.

**Provincial/legislated services –** additional funding requirements resulting from provincial legislation or regulations that:

- Increase the cost of providing existing programs and services at current service levels
- Result in the implementation of a new program, or
- Enhance the service level of an existing program or service

Pay increases from collective bargaining for employees delivering provincially mandated cost-shared programs and services are also included in this category. Budget pressures have ranged from $4 to $8 million in the last two years.

**Costs of growth –** additional resources required to provide services to address growth in the population of the City each year, and to service the new infrastructure and equipment added to the City's inventory as a response to population growth. In the last two years, growth-related costs added from $7 to $15 million to the operating budget. These expenses were predominantly due to expansion in the City's transit and road systems.

**Service level improvements –** additional resource requirements to provide new programs and services to businesses and residents, or to provide a higher level of service for existing Council-approved programs and services. Improvements include increases to the contribution towards the City's capital program. Either Council approves these service-level enhancements during the course of the year, or improvements are recommended as part of the City Corporate Plan. In the last two years, the cost of Council-approved enhancements has added $21 million to the City budget.

## OPERATING FORECAST FOR 2007

The 2006 Draft Budget Summary presented a forecast of the cost pressures and resulting impact on property taxes for 2007. A tax increase of 8% was projected, based on the following assumptions:

- Costs to provide all programs and services at current levels are presented in the maintain existing services category
- Compensation increases were based on bargaining mandates plus forecasted cost of salary increments, and corresponding employee benefit cost increases
- General inflation was projected at 2% per year (except for energy costs at 7%)
- An increase in the winter maintenance provision will be required to deal with additional winter storm events
- No forecasted increase in Ontario Works (welfare) caseload

- An annual increase in Ontario Disability Support Payments of 2.9%
- User fee increases set to maintain cost-to-revenue relationship, with increases to transit fares to achieve Council-directed target of 55% of direct operating cost
- Increases to garbage collection costs, plus landfill closure liability costs, to be recovered through an increase to the garbage collection fee
- Assessment growth of 2% per annum
- Provincial cost-shared program funding continues at current levels except for increases announced for public health and paramedic services
- Annual increases to reflect estimated operating impacts from legislative changes
- Annual increases to reflect estimated operating impacts of growth
- Annual increases to contribution to capital reserves based on the Infrastructure Construction Price Index
- Annual increase equivalent to a 1% tax increase to address strategic initiatives capital projects
- Annual increase equivalent to a 1% tax increase to address Council-determined priorities and enhancements to services
- No new sources of revenue or new taxation powers
- Ottawa Police Service increases as provided by Police finance staff
- Tax rate increase based on the total 2006 taxation assuming that a 1% increase will generate 1% of the total 2006 taxation

| As originally presented in the 2006 budget | 2007 ($ thousands) |
|---|---|
| Maintain existing services | 58,500 |
| Provincial/legislated services | 6,000 |
| Costs of growth | 10,000 |
| User fees | (10,000) |
| Assessment growth | (19,000) |
| Efficiencies target | (5,000) |
| | **40,500** |
| | |
| Enhancements – Capital strategic initiatives | 9,500 |
| Enhancements – Operating budget | 9,500 |
| One-time transfer from tax stabilization reserve in 2006 | 1,000 |
| | **60,500** |
| | |
| **Ottawa Police Service** | **15,800** |
| **Original estimated taxation increase** | **76,300** |
| | |
| **Tax rate increase** | **8.0%** |
| | |
| **Changes in forecast assumptions** | |
| Higher base pressures | 3,862 |
| Higher growth pressures | 5,055 |
| Lower mandatory pressures | (1,365) |
| Defer increase in efficiency target for one year | 5,000 |
| One time 2006 provincial funding | 20,000 |
| Continuation of Ontario Municipal Partnership Fund funding | (1,455) |
| Additional Ontario Municipal Partnership Fund funding per provincial budget | (4,500) |
| Additional paramedic funding per provincial budget | (5,300) |
| Change in forecast as provided by Ottawa Police Service | (2,250) |
| **Total changes** | **19,047** |
| **Tax impact of adjustments** | **2.0%** |
| | |
| **Revised taxation increase** | **95,347** |
| **Tax rate impact** | **10.0%** |

## ADJUSTMENTS TO THE LRFP II FORECAST

**Higher base pressures –** Based on departmental reviews of projected cost pressures for 2007, the requirements for 2007 to provide and maintain existing services have increased.

**Higher growth pressures –** The revised amount forecasted for growth pressures will more accurately address operational requirements due to infrastructure and population increases.

**Lower provincial mandatory, cost-shared programs pressures –** The original forecast was based on recent experience during the 2005 and 2006 budget cycles. Ontario Disability Support case loads and support payments along with prescription drugs are projected to increase at rates higher than inflation. Per diem rates and operating subsidies in the housing program are projected to increase at rates higher than originally projected. Offsetting these increases are decreases in the Ontario Works case load along with higher subsidies for administration costs.

**Efficiency target –**The $5 million increase to the 2007 target is recommended for deferral. The June 30, 2006 Operating Status Report identified that a significant portion of the 2006 corporate efficiency and overtime targets totalling $12.9 million will not be achieved in 2006. Any remaining balance will be carried forward for achievement in 2007. The Branch Process Review Program (BPRP), which is designed to uncover these efficiencies, started in 2006 with two pilot reviews. Next year, the BPRP will review six branches. Deferring the $5 million increase in the efficiency target for one year will allow the projected savings to match the target and prevent a deficit within the year.

**Increase in contribution to capital from the operating budget –** Council policy states that annual contributions to the City's capital reserves are to increase by the City's Infrastructure Construction Price Index. The original forecast assumed an increase of 2%. However, the 2005 index has been calculated by Statistics Canada at 5.1%. This reflects the significant increases that are occurring for construction materials such as steel, asphalt, copper and fuel. The 2007 forecast has been revised to include this increase.

**One-time provincial funding –** In 2006, the City budgeted for and the Province provided an additional $20 million to the City, $10 million of which was allocated for transit operating requirements. There has been no indication that this transit funding will be provided on a permanent basis.

**Ontario Municipal Partnership Fund funding to continue at an increased level –** In the LRFP II forecast it was projected this grant would be eliminated as per the original announcement in 2005. The 2006 provincial budget reinstated this program and the City will receive an additional $4.5 million based on social service program costs. The forecast for 2007 was revised to include increased funding.

**Additional paramedic funding –** The 2006 provincial budget indicates that the Province will phase in additional funding to achieve 50/50 program cost sharing. For 2007, this will result in an additional $5.3 million in provincial revenues.

## OPERATING BUDGET FORECAST FOR 2008 TO 2010

The changes to the original 2007 budget forecast identified above have been reflected in the development of forecasts for the 2008 to 2010 period. As with most forecasts, the ability to make meaningful, accurate cost pressure projections decreases as forecasts are extended into the future years.

| | 2008 ($ thousands) | 2009 ($ thousands) | 2010 ($ thousands) |
|---|---|---|---|
| Maintain existing services and levels | 55,000 | 58,000 | 61,000 |
| Provincial/legislated services | 6,000 | 7,000 | 8,000 |
| Costs of growth | 15,000 | 17,000 | 19,000 |
| User fees | (10,000) | (10,000) | (10,000) |
| Assessment growth | (20,000) | (20,000) | (20,000) |
| Efficiencies target | (5,000) | - | - |
| | **41,000** | **52,000** | **58,000** |
| | | | |
| Enhancements – Capital strategic initiatives | 10,000 | 10,500 | 11,000 |
| Enhancements – Operating budget | 21,200 | 17,500 | 11,000 |
| | **72,200** | **80,000** | **80,000** |
| | | | |
| **Ottawa Police Service** | **15,000** | **16,800** | **15,800** |
| **Estimated taxation increase** | **87,200** | **96,800** | **95,800** |
| | **8.2%** | **8.3%** | **7.5%** |

The forecast tax increases listed above were based upon the following assumptions:

- Costs to provide all programs and services at current levels are presented in the maintain existing services category
- Compensation increases were based on bargaining mandates where known, or on the forecasted Ottawa inflation rate plus forecasted cost of salary increments, and, corresponding employee benefit cost increases
- No benefit rate increases have been forecast; the benefit to compensation ratio has been kept constant for the forecast period
- General inflation projected at 2.3% for 2008, 2.4% for 2009 and 2.1% for 2010, reflecting the Conference Board of Canada's Metropolitan Outlook forecast (autumn 2006)
- Energy costs projected at 7%
- Winter maintenance provision maintained at 2007 level, assuming that 2008 to 2010 will be within the established three-year average
- User fee increases set to maintain cost-to-revenue relationship along with increases to transit fares to achieve Council-directed target
- Increases to garbage collection costs are to be recovered through an increase to the garbage collection fee

- Assessment growth has been maintained at $20 million each year, which represents 2% in 2008
- Provincial cost-shared program funding continues at 2007 levels
- Annual increases in Ontario Disability Support Payments (ODSP) at 2%, with a 3% annual increase in ODSP caseload
- Annual increases of 6% for the Employment and Financial Assistance's prescription drugs program and annual increases of 2% in the Ontario Works rate
- Annual 2.1% increases for rent supplement programs and annual 3.2% increases for costs associated with the public housing program
- Provincial/legislated program estimates include compensation increases based on bargaining mandates where known, or on the forecasted Ottawa inflation rate plus forecast cost of salary increments; and, corresponding employee benefit cost increases
- Annual increases reflect estimated operating impacts of growth plus estimated operating costs for Light Rail Transit, starting in 2009, as identified in the Council-approved report on the North-South Light Rail Transit Project. Any adjustment to the timing will be reflected in future forecasts
- Annual increases to contribution to capital reserve funds based on estimated Infrastructure Construction Price Index (2.4% for 2008, 2.7% for 2009 and 3.4% in 2010)
- Annual increase equivalent to a 1% tax increase to address strategic initiatives capital projects
- Annual increase equivalent to a 1% tax increase to address Council-determined priorities and enhancements to services, plus amounts for the solid waste organics program in 2008 and 2009
- No new sources of revenue or new taxation powers
- Ottawa Police Service increases as provided by police finance staff
- Any one-time grants received to be pursued on a permanent basis

# OPTIONS TO ADDRESS BUDGET FUNDING GAP

## Potential short-term solutions

**1) Reduce or eliminate funding for program and service enhancements**

The four-year forecast provides for annual increases of $9.5 to $11 million (representing a 1% annual tax increase) to address potential Council-directed enhancements. Enhancements are at the discretion of Council and can therefore be reduced or eliminated by Council. However, reducing or eliminating program and service improvements can limit the City's ability to address community priorities.

**2) Reduce or eliminate funding for some capital projects or finance an increase in the capital program with debt**

The four-year forecast provides for annual increases of $9.5 to $11 million (representing a 1% annual tax increase) to fund capital strategic initiatives projects in support of the City's Corporate Plan. Reducing or eliminating this funding will limit Council's ability to address the Corporate Plan agendas and community expectations. As an alternative, 10-year debt financing on an annual strategic initiatives budget of $9.5 million would result in annual debt servicing costs of $1.2 million.

**3) Pursue the Province to address cost-sharing shortfalls or provide other grants**

The funding shortfall on cost-sharing arrangements for existing programs is approximately $16 million. The City will continue to work with the Province to obtain adequate funding for cost-shared programs.

**4) Use of the provincial gas tax to replace one-time transit funding**

The rules for the use of the gas tax revenues have been modified. They now allow these revenues to be applied against transit operating costs regardless of whether they enhance ridership. Allocating $10 million of gas tax revenues to fund transit operating costs will reduce the amount available to fund transit capital requirements.

**5) Property tax increases above the rate of inflation**

In the absence of other provincial or federal revenue sources or service level reductions, increasing property tax above the rate of inflation will provide additional funding to minimize the impact on current service levels.

**6) Increase user fees more than the rate of inflation or introduce new user fees**

Increasing user fees at more than the rate of inflation has the potential to make City services unaffordable to some residents, potentially resulting in lower usage and lower revenues. The City has introduced new user fees over the past several years to assist in recovering program costs. However, opportunities to generate additional revenues under the current legislative framework are limited.

**7) Reduce current service levels**

Council has the ability to review current service levels and reduce services. However, it should be noted that in the 2004 EKOS survey, the vast majority of residents indicated that City services should be maintained or expanded.

## Potential longer-term solutions

### 1) Eliminate funding shortfalls on provincial cost-shared programs – seek new revenue sources or powers

Through the Association of Ontario Municipalities, the City will strongly encourage changes as part of the recently announced Provincial-Municipal Fiscal and Service Delivery Review to improve the delivery and funding of municipal services. However, the report is not scheduled to be released until the spring of 2008. In the interim, the City will continue to work with the provincial government to reduce funding shortfalls on cost-shared programs and propose new revenue sources.

### 2) Pursue provincial and federal governments for stable, predictable funding

A number of federal and provincial programs have emerged over the past few years to help municipalities address capital infrastructure requirements. The City will continue its best efforts to obtain stable, predictable funding to address operating responsibilities.

### 3) Defer growth-related projects

Growth-related infrastructure results in ongoing maintenance and programming cost pressures on the City's operating budget. The process to begin revising the City's Official Plan will start in late 2007, with completion in 2008. The process to enact a new *Development Charge By-law* by 2009 will also commence in 2008. Subject to growth projections and infrastructure requirements, delaying the construction of new infrastructure may be feasible without significantly affecting public expectations.

The options presented above will need to be considered by Council as it provides direction for the preparation of the 2007 to 2010 budgets.

# CAPITAL FORECAST – CAPITAL REQUIREMENTS FUNDED FROM TAXATION

Since amalgamation, Council has directed staff to prepare three 10-year capital forecasts to help the City better plan and manage capital projects. Similar to LRFP I and II, the LRFP III analysis includes capital projects funded through taxes. Water and sewer capital projects, which are funded through the water rate, are analyzed separately in this document. Capital projects for the Ottawa Police Service are also excluded and will be provided separately by the Police Services Board.

LRFP III identifies the City's capital requirements from 2007 to 2016. Similar to LRFP II, capital requirements have been grouped into three broad capital project categories to allow Council to prioritize funding. Different funding is available for different kinds of projects, and strategies to address funding gaps may vary between categories. The categories are:

**1) Renewal of City assets –** This category reflects funding required to maintain and/or replace existing capital assets throughout the full life of those assets. These assets include buildings, structures, roadways, bridges, vehicles, and equipment.

**2) Growth –** This category includes projects that were identified in the Development Charges Background Study that align with the goals contained in the City's Official Plan. More specifically, growth projects must have a development charge component that is greater than 30% of the total amount requested. This means developers must pay more than 30% of the cost of the project for it to be considered a capital growth project. Projects where the development charge component is 30% or less are usually categorized as renewal of City assets or strategic initiatives.

**3) Strategic initiatives –** This category includes Council-directed initiatives identified in the City Corporate Plan. These initiatives include projects that implement City master plans and the Ottawa 20/20 Plan, and can be designed to acquire environmental areas or enhance services currently being provided to residents. Also included are management initiatives to enhance organizational effectiveness, implement new legislative requirements, and respond to changes in demand for service. As identified previously, there are now more projects categorized as strategic initiatives due to the reduced number of services eligible for funding through development charges.

Since LRFP II was adopted in 2004, the City has moved the garbage collection component of solid waste services from the tax bill to a separate user fee. This user fee will become part of the water and sewer bill in January 2007. As taxes are no longer the source of funding for this service, the needs and funding analysis for this component of solid waste is provided in a separate section. Transit capital needs and funding analysis are also separate, as contributions to transit capital are not raised from city-wide taxes. All other capital needs funded from city-wide taxes are consolidated in the last section.

## CHANGES IN REVENUE SINCE LRFP II

When it was presented to Council in the fall of 2004, LRFP II outlined capital projects requiring funding from taxes for 2005 to 2014. The plan included a number of new non-tax capital revenue sources announced in 2004. Assumptions were made about how these new funding sources would be applied and the amount they would generate for use over the 10-year forecast period. The difference between capital needs and estimated revenue was projected to be $757 million over the forecasted 10-year period.

There have been a number of revisions to revenue assumptions since LRFP II was adopted by Council. Major revisions have resulted from provincial and federal announcements, including municipal use and funding levels of gas tax revenues, clarification of treatment of the GST rebate, and establishment of the Hydro Ottawa endowment fund with its potential rate of return. A description of these changes and their impact on the projected LRFP II funding gap is presented below.

### Provincial gas tax

The 2004 assumptions about the provincial gas tax were that Ottawa would be able to access $350 million over the 10-year period. The entire amount was to be used in the capital program, either as a direct cash contribution, or to service debt issued to fund transit capital projects. The Province issued guidelines around the use of gas tax revenues shortly after Council approved LRFP II. These guidelines permitted the funds to be used only for increased transit operating requirements resulting from projects to increase ridership and for capital initiatives. Using these guidelines, Council permanently included $2.1 million in 2005 and a further $5 million in 2006 in the operating budget to fund transit. Applying this revenue to the operating budget, rather than the planned capital budget, means the capital funding gap forecast in LRFP II has increased by $66 million.

### Federal gas tax

When LRFP II was presented in 2004, the federal government had just announced it would be contributing a portion of its gas tax revenues to municipalities. The allocation of funds was assumed to be based on a combined transit ridership and per capita basis. It was also assumed funds could be used for capital needs to support all forms of transportation, including roads and bridges. The actual agreement for the transfer of these funds and the application rules were not known until mid-2005.

The first change to affect the LRFP II forecast was that funds would be allocated to each city on a per capita basis only. This reduced the amount the City had forecast by $60 million from 2005 to 2014. In late 2005, the federal government agreed to increase the gas tax transfer for 2006 and 2007, which again changed the forecast revenue and reduced the total funding shortfall to $20 million over the 10-year period. This shortfall increased the net gap forecast in LRFP II.

The second funding change to affect the LRFP II forecast was that the federal gas tax could only be used for capital works in transit, water and wastewater, community energy systems and solid waste. The City funds water and wastewater from the water bill and was already implementing a strategy to deal with capital requirements for that area. Solid waste did not have a significant capital funding problem. This left transit as the only area that could benefit from these funds.

As mentioned previously, the assumptions on how to apply the federal gas tax were much broader in LRFP II. In that plan, $100 million in gas tax-supported debt was applied to non-transit projects. These projects, primarily roads and bridges, are not eligible for funding through the federal gas tax. The direct impact of this change is that the capital funding gap increased by $100 million.

The Municipal Funding Agreement Guide for the Federal Gas Tax, which was issued by the Association of Municipalities in Ontario in October 2005, included the following requirement:

> "Canada and Ontario have agreed not to reduce other infrastructure funding sources and municipalities are agreeing not to displace current capital investment or use the revenue to reduce municipal taxes. The revenue must result in increased investment in environmentally sustainable municipal infrastructure equal to the amount of revenue received."

To ensure the City complies with this clause, reporting requirements have been put in place to monitor the City's capital investment in eligible areas where the gas tax is applied. Contributions to capital from the transit levy cannot be reduced without jeopardizing federal gas tax revenues. The result is that $661 million in federal gas tax debt for transit is no longer needed, since maximizing debt does not free up funds for other non-transit capital works. As this money is no longer available for roads, bridges and other non-transit capital projects, the capital funding gap has increased by $336 million.

### Goods and Services Tax (GST)

In 2004, the federal government announced that municipalities would be rebated the full 7% GST, instead of only 4%. Initially, the federal government kept the additional 3% rebate separate from the other 4% and provided it to municipalities as an unconditional grant. LRFP II assumed that the federal government would continue this practice and contribute $170 million to the City of Ottawa over the 10-year period.

Instead, the federal government started combining the two rebates into one in 2005 and the City was no longer able to record the additional rebate as revenue. As a result, the contribution to capital has increased and the cost of projects has decreased for a combined value equal to the forecast.

## Development charges

LRFP II was aligned with the Development Charge Background Study and its recommendations as presented to City Council on July 14, 2004. On December 8, 2004, City Council approved revisions to the Study, which reduced development charges and the amount available to fund the growth portion of capital projects. The decrease in development charge revenue is estimated to be $41 million over the 10-year period, which increases the City's funding portion of growth-related capital projects.

## Hydro Ottawa endowment fund and Ottawa Hydro dividends

LRFP II recommended the creation of an endowment fund to invest the proceeds of the Hydro Ottawa refinancing ($200 million). It also recommended special legislation allowing investment in a broader range of financial instruments than is allowed under the Municipal Act. The special legislation was approved in December 2005 and the fund was established. An assumption was made in the LRFP II that the fund would have an investment return of 10% for capital projects. However, a more attainable target of 6.5% was established in June 2006 to ensure preservation of the initial $200 million investment. This reduced the amount available for capital projects by $83 million over the 10-year LRFP II period.

Assumptions regarding the Ottawa Hydro dividends also changed, resulting in a $7 million reduction in the forecast revenue over the 10-year period. This reflects actual dividends received, which are dependent on Ottawa Hydro's financial performance.

## Contribution to capital

Each year, the City dedicates a portion of taxes as a contribution to funding for capital projects. LRFP II assumed contributions to capital would grow by 2% over 10 years to reflect annual inflation. This added $91 million over the 10-year period. However, costs associated with capital projects were not increased by inflation. LRFP II assumed the entire increase in the contribution would be offset by the increases in cost over time. Therefore, to ensure the costs and revenues are valued at the same time, the $91 million increase has been removed.

The actual decrease to the contribution to capital is only $11 million over the 10-year period, as the elimination of the assumption made about inflation is partially offset by the $80 million increase from GST revenues.

In summary, by re-stating the funding gap of $757 million in LRFP II to reflect changes in the way non-tax revenue can be used, together with the changes in assumptions made in the fall of 2004, the gap between the funding requirement for capital projects and the amount available increases to $1,401 million over the same 10 years. The following table itemizes these changes.

| | As per LRFP II ($ millions) | LRFP II Re-stated to reflect changes ($ millions) |
|---|---|---|
| **Gross City tax-supported capital requirement** | **7,584** | **7,494** |
| Less: | | |
| • Revenues | 1,708 | 1,708 |
| • Development charges | 1,889 | 1,848 |
| **Net City tax-supported capital requirement** | **3,987** | **3,938** |
| Less: | | |
| • Contributions to capital from taxation | 1,113 | 1,102 |
| • Revolving debt | 400 | 400 |
| • GST rebate | 170 | 0 |
| • Hydro dividends | 57 | 50 |
| • Hydro endowment fund interest | 200 | 117 |
| • Provincial gas tax | 350 | 284 |
| • Federal gas tax | 435 | 415 |
| • Gas tax-supported debt | 761 | 365 |
| • Debt servicing from gas tax | (256) | (196) |
| **Total needs not met (funding gap)** | **757** | **1,401** |

## LRFP III – CHANGES IN GROSS CAPITAL NEEDS SINCE LRFP II

There have been a number of adjustments made to the capital needs identified in LRFP II's 10-year period. A comparison of gross costs, which includes projected revenues and development charges identified in LRFP II and the 10-year period for LRFP III, is shown below.

| Category | Re-stated LRFP II ($ millions) | LRFP III ($ millions) | Change ($ millions) |
|---|---|---|---|
| Renewal of assets | 2,399 | 2,681 | 282 |
| Growth | 4,003 | 2,809 | (1,194) |
| Strategic initiatives | 1,092 | 1,262 | 170 |
| **TOTAL** | **7,494** | **6,752** | **(742)** |

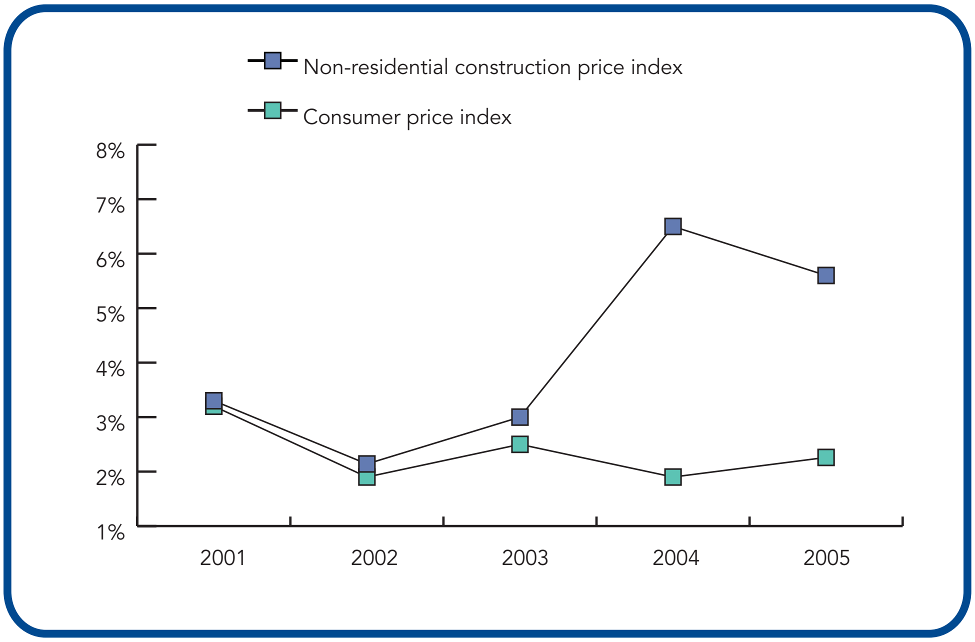
While the total capital funding needs have decreased, the capital funding needs in the renewal and strategic initiative categories have increased. An explanation of the changes affecting each category is provided below.

### Inflation pressures within the construction industry

The City's capital projects are delivered by the Ottawa construction sector. The construction industry is subject to price increases that vary significantly from those experienced by most residential consumers. Statistics Canada reported that the Consumer Price Index for the Ottawa-Gatineau metropolitan area increased by 9.1% from 2001 to 2005. At the same time, the non-residential Building Construction Price Index (relates to cost increases in the construction of industrial, manufacturing and institutional structures) increased by 18%, with the largest increases occurring in the last two years.

The following graph shows the percentage change in these two indexes from 2001 to 2005.

## Yearly change in Ottawa index




The non-residential Building Construction Price Index increased by almost twice the Consumer Price Index. However, the impact on construction costs can be much more significant (depending on the type of project), as contractors have had to deal with large variations and increases in the cost of construction materials. Examples of materials typically used in City capital projects, and what has happened to prices of each, are listed below (all increases are in Canadian dollars).

1) **Steel – Rebar –** Pricing fluctuations of more than 20% have resulted since a major price increase in late 2004. Rebar is a significant component in retaining walls, bridges, etc. The City purchases approximately 500 tonnes of reinforcing steel every year.

2) **Asphalt –** The cost of asphalt has increased by an estimated 15% between 2004 and 2005. From 2005 to 2006, it increased by another estimated 20%. The City purchases approximately 200,000 tonnes of asphalt per year.

3) **Concrete –** Cement powder and the price of concrete have increased 10-13% from October 2004 to October 2005. This material is a major component of bridges, structures, and sidewalks. The City purchases approximately 7,500 cubic metres of concrete every year.

4) **Petroleum prices –** Petroleum prices have increased 20-30% over the last year. This has had a major impact on costs, as fuel represents a high percentage of trucking and equipment operations. Oil is also a major component of asphalt; it has doubled in price in 2006.

The funding needs in LRFP II were identified in early 2004 and reflected prices known at that time. LRFP III reports project costs in 2006 dollars. Due to inflation, most projects have increased between 5% and 10%, depending on their nature. Inflation is estimated to have added more than $200 million to the cost of capital projects required in the next 10 years.

### Additional projects resulting from new initiatives or information

When LRFP II was presented, not all asset management plans had been completed. For example, the recently completed asset management plan for the City's parks identified an additional $100 million in renewal needs over 10 years.

Many new projects in the strategic initiatives category have been initiated since LRFP II. They include:

- Replacement of the main library – total increase of $154 million in 2011 and 2012
- Solid waste facility upgrade program – $100 million identified in 2016
- Vulnerable buildings strategy – increase of $19 million over the next 10 years to ensure the City's most needy buildings receive required maintenance
- Urban natural features initiative – increase of $38 million over the LRFP III 10-year period. In LRFP II, staff submitted an estimated 10-year requirement of $8.3 million. They did this without the benefit of the Urban Natural Areas Environmental Study (UNAEES), which was underway. The $38 million in LRFP III is based on a list of specific land parcels recommended for protection.

### Affordable housing funding

LRFP II set a target to develop 500 affordable housing units a year for the subsequent 10 years. The average annual capital funding requirement was also estimated at up to $36 million for the 10-year LRFP II timeframe. This estimate was contingent on matching funding from federal and provincial governments. At the time, there was no federal or provincial funding program in place.

Since then, the Province of Ontario introduced the Affordable Housing Program (AHP), signalling the return of the federal and provincial governments to funding for housing after an absence of more than 10 years. The AHP provides federal and provincial funding to support the provision of new affordable housing. The City of Ottawa participated in the pilot phase of this program in 2004 and matched federal and provincial capital funds to support the development of 271 new housing units. In 2006, the AHP was revised, with the Province now fully matching the federal share. Total current AHP funding to Ottawa is $30.16 million, in three streams: home ownership grants up to $10,000 per unit (232 units); housing allowance subsidies up to $250 per month for five years (400 units); and, rental and supported housing grants up to $70,000 per unit for new development (315 units).

The City has been using funds in the Social Housing Reserve to match the AHP funding for the rental and supported housing stream, bringing the total per unit funding up to an average of $90,000 (varies between projects). This additional funding enables the program to reach the low-income targets established in Action Ottawa — 60% of the units must be rented to low-income households. To produce rents suitable to low-income households, Action Ottawa unit rents will not exceed 70% of the average market rent. Funding for 139 of the 315 AHP units was allocated in October 2005. The remaining 176 units will be allocated in 2007, subject to provision of an additional $1.3 million in capital funding in the 2007 budget.

LRFP III also projects the possible continuation of the AHP to 2013. Based on current information, the City can expect funding from the AHP for 80 additional affordable housing units in 2008. If the federal government delivers on its stated commitment in Bill C-48 for an additional $800 million in funding for affordable housing, it is possible the City could receive funding for approximately 90 units per year until 2013. To ensure these funds are able to meet the Action Ottawa low-income targets, the City would be required to contribute additional funding, approximately $18 million over six years. This projection reflects reliance on federal and provincial funding and clearly demonstrates the gap between that funding and the benchmark target of 500 units per year.

### Advancement of the capital growth agenda

The capital growth category has decreased since LRFP II. In 2005 and 2006, $1,156 million in growth projects were authorized, compared to $860 million identified in LRFP II. The increase of $296 million was due to projects on the 10-year list advancing their start date. This reduces the capital growth requirement for the next 10 years by the same amount.

In LRFP II, growth projects were identified from the Development Charges Background Study and were not timed to coincide with the receipt of the development charges. The new development charge funding policy, approved by Council in May 2006, provides a basis for determining when budget authority for projects may be put in place. Under this funding policy, the amount of development charges that must be collected for a project to proceed is linked to the timing of the project in the whole development cycle. For projects such as recreation facilities, which are built towards the end of the development cycle, the development charges must have been collected prior to a request for project authority. Other capital projects, such as sewers, could be constructed prior to collecting the entire amount of the development charge. The result of implementing this funding policy is that there are fewer growth projects. The development community has indicated they are supportive of the current Council process.

The development charge funding policy recognizes that certain infrastructure must be put in place prior to the development that generates the development charge revenue. The funding policy was implemented to ensure the City is meeting the demand for capital growth projects, while minimizing the risk of building too far ahead of receiving the development charges to pay for the project.

### Change in the net City requirement

| | LRFP II (restated) ($ millions) | | LRFP III ($ millions) | | % Reduction from gross to net | |
|---|---|---|---|---|---|---|
| | Gross | Net | Gross | Net | LRFP II | LRFP III |
| Renewal of assets | 2,399 | 2,277 | 2,681 | 2,483 | 5% | 7% |
| Growth projects | 4,003 | 820 | 2,809 | 862 | 80% | 69% |
| Strategic initiatives | 1,092 | 841 | 1,262 | 1,132 | 23% | 10% |
| TOTAL | 7,494 | 3,938 | 6,752 | 4,477 | 47% | 34% |

LRFP II presented the City's net capital costs, which represent the remaining City funding requirement once revenues and development charges are deducted. The change in the net capital costs since LRFP II is shown in the table above.

The change in the gross amount of required capital funding does not always translate into a corresponding change in the amount the City must fund. The gross capital cost has decreased from LRFP II to LRFP III. However, the net amount to be funded from the City has increased. This is primarily due to the change in the types of projects that are proposed under the growth category. Every service eligible for development charge funding has a component funded from development charges and another amount funded by the City. The percentage funded by the City varies with the type of project. For example, some transit growth projects require 85% City funding, whereas road projects only require 5% City funding. The realignment of growth projects has resulted in the decrease of gross costs, but the net City funding requirement remains fairly constant.

The other change in revenue assumptions is in the strategic initiative category. In LRFP II, the inclusion of $403 million in social housing needs, 50% of which was to be funded from other levels of government, reduced the net requirement. The gross social housing forecast has now been reduced to $98 million. New projects added to the list do not have any revenue sources associated with them. As a result, the net City cost for strategic initiative projects has increased.

Overall, the City has to fund an additional $539 million in capital costs due to the change in the projects included in the forecast and the revenue and development charges associated with each.

## TEN-YEAR FORECAST OF NEEDS AND REVENUES – TRANSIT SERVICES

As part of the light rail transit discussion, an analysis of transit capital needs and funding was presented to Council. That analysis was built on information available at the time. Information presented here, while very similar, reflects the work that went into creating LRFP III. The forecast has not changed, as transit capital needs can be met within the next 10-year period.

### Ten-year forecast of needs and revenues – Transit ($ millions)

| | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Renewal** | | | | | | | | | | | |
| Needs | 42 | 64 | 75 | 40 | 35 | 28 | 20 | 66 | 137 | 152 | 659 |
| Funding | | | | | | | | | | | |
| Revenues (fed & prov) | 10 | 18 | 22 | 10 | 9 | 7 | 4 | 19 | 42 | 47 | 188 |
| Federal and provincial gas tax | 28 | 12 | 39 | 29 | 25 | 21 | 16 | 38 | 35 | 11 | 254 |
| Contribution to capital | 4 | 33 | 14 | 1 | 1 | – | – | 9 | 60 | 94 | 216 |
| Revolving debt | – | 1 | – | – | – | – | – | – | – | – | 1 |
| | 42 | 64 | 75 | 40 | 35 | 28 | 20 | 66 | 137 | 152 | 659 |
| *Funding gap* | – | – | – | – | – | – | – | – | – | – | – |
| **Growth** | | | | | | | | | | | |
| Needs | 120 | 93 | 135 | 248 | 60 | 112 | 202 | 264 | 503 | 383 | 2,120 |
| Funding | | | | | | | | | | | |
| Revenues (fed & prov) | 13 | 14 | 65 | 144 | 11 | 74 | 140 | 142 | 274 | 169 | 1,046 |
| Federal and provincial gas tax | 12 | 37 | 13 | 23 | 27 | 25 | 31 | 20 | 15 | 19 | 222 |
| Federal and provincial gas tax debt | 72 | 15 | 3 | 6 | 8 | – | – | 34 | 83 | 18 | 239 |
| Development charges | 23 | 20 | 16 | 42 | 10 | 13 | 23 | 30 | 65 | 55 | 297 |
| Contribution to capital | – | – | 4 | 8 | – | – | – | 3 | 33 | 89 | 137 |
| Revolving debt | – | 7 | 34 | 25 | 4 | – | 8 | 35 | 33 | 33 | 179 |
| | 120 | 93 | 135 | 248 | 60 | 112 | 202 | 264 | 503 | 383 | 2,120 |
| *Funding gap* | – | – | – | – | – | – | – | – | – | – | – |
| **Strategic Initiatives** | | | | | | | | | | | |
| Needs | 12 | 7 | 4 | 2 | 2 | 2 | 2 | 2 | 3 | 20 | 56 |
| Funding | | | | | | | | | | | |
| Federal and provincial gas tax | 10 | 5 | 2 | – | – | – | – | – | 1 | 18 | 36 |
| | 10 | 5 | 2 | – | – | – | – | – | 1 | 18 | 36 |
| *Funding gap* | *2* | *2* | *2* | *2* | *2* | *2* | *2* | *2* | *2* | *2* | *20* |
| **All categories** | | | | | | | | | | | |
| Needs | 174 | 164 | 214 | 290 | 97 | 142 | 224 | 332 | 643 | 555 | 2,835 |
| Funding | | | | | | | | | | | |
| Revenues (fed & prov) | 23 | 32 | 87 | 154 | 20 | 81 | 144 | 161 | 316 | 216 | 1,234 |
| Federal and provincial gas tax | 50 | 54 | 54 | 52 | 52 | 46 | 47 | 58 | 51 | 48 | 512 |
| Federal and provincial gas tax debt | 72 | 15 | 3 | 6 | 8 | – | – | 34 | 83 | 18 | 239 |
| Development charges | 23 | 20 | 16 | 42 | 10 | 13 | 23 | 30 | 65 | 55 | 297 |
| Contribution to capital | 4 | 33 | 18 | 9 | 1 | – | – | 12 | 93 | 183 | 353 |
| Revolving debt | – | 8 | 34 | 25 | 4 | – | 8 | 35 | 33 | 33 | 180 |
| | 172 | 162 | 212 | 288 | 95 | 140 | 222 | 330 | 641 | 553 | 2,815 |
| *Funding gap* | *2* | *2* | *2* | *2* | *2* | *2* | *2* | *2* | *2* | *2* | *20* |

## Assumptions for transit services

In building the revenue forecast, a number of assumptions were made, as detailed below:

- Projects that would fall into the strategic initiatives category were not funded if they required funds from contribution to capital. Council will deal with all strategic initiatives projects as part of the City Corporate Planning process.
- Over the 10-year period, provincial gas tax funding is valued at $373 million, $71 million of which will be transferred to the operating budget and $173 million will be used to service previously authorized or planned debt. This leaves $129 million over the 10-year period to be used as cash contributions to capital or for operating requirements as allowed. In this plan, all available provincial gas tax revenues have been applied to capital.
- Over the 10-year period, federal gas tax revenues are assumed to be $468 million, $85 million of which will be used to service previously authorized or planned debt. This leaves $383 million to be used for transit-related capital projects. The full $383 million is forecast to be spent in the 10-year period.
- Tax-supported debt is referred to as "revolving debt," as it replaces paid debt with new debt. The annual amount of tax-supported revolving debt is assumed to be $40 million per year or $400 million over the 10-year period. In total, $180 million of the $400 million in revolving debt is applied to transit.
- New debt that is beyond the amount covered by the current debt servicing budget is assumed to be repaid from gas tax revenues or other non-tax sources. This is consistent with the LRFP II funding strategy.
- It is assumed that growth-related projects identified in 2010 and later (beyond the current term of the Development Charge By-law) that are eligible for development charge funding will be included in subsequent terms of the By-law. In addition, debt repayments on current-term growth projects are assumed to be included in the next term of the By-law.
- It is assumed that revenues and subsidies for transit projects from other levels of government totalling $1,234 million over the 10-year period will continue. Consistent with past practice, if these revenues or subsidies are not secured at the time of project approval, the project will either be deferred or project spending will occur only when the revenues are secured.
- Consistent with Council direction, the minimum reserve fund balance is $50 million for all tax-supported reserve funds, including the transit reserve fund. As contributions to the transit capital reserve are restricted from being spent on non-transit projects, the tax-supported reserve balances will exceed $50 million by an additional $41 million over the 10-year period with the surplus going to the transit reserve fund.

- As approved by Council, contributions to capital have been increased by the Infrastructure Construction Price Index (5.1%) in 2007, but remain constant over the remaining nine-year period.
- It is assumed that the second phase of the Light Rail Transit project will be cost-shared with the provincial and federal governments at one-third for each level of government.

## TEN-YEAR FORECAST OF NEEDS AND REVENUES – SOLID WASTE SERVICES

The garbage collection and disposal program is now funded through the garbage user fee. To recognize the unique source of funds for this service, the capital needs and funding have been identified separately.

### Ten-year forecast of needs and revenues – Solid waste services ($ millions)

| | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Renewal** | | | | | | | | | | | |
| Needs | 1 | 3 | 1 | – | 1 | – | – | 1 | – | – | 7 |
| Funding | | | | | | | | | | | |
| Contribution to capital | 1 | 1 | 2 | 1 | 1 | – | – | 1 | – | – | 7 |
| | 1 | 1 | 2 | 1 | 1 | – | – | 1 | – | – | 7 |
| *Funding gap* | *–* | *2* | *(1)* | *(1)* | *–* | *–* | *–* | *–* | *–* | *–* | *–* |
| **Strategic initiatives** | | | | | | | | | | | |
| Needs | 10 | 2 | 5 | 1 | 3 | 1 | 4 | 1 | 3 | 101 | 131 |
| Funding | – | – | – | – | – | – | – | – | – | – | – |
| | – | – | – | – | – | – | – | – | – | – | – |
| *Funding gap* | *10* | *2* | *5* | *1* | *3* | *1* | *4* | *1* | *3* | *101* | *131* |
| **All categories** | | | | | | | | | | | |
| Needs | 11 | 5 | 6 | 1 | 4 | 1 | 4 | 2 | 3 | 101 | 138 |
| Funding | | | | | | | | | | | |
| Contribution to capital | 1 | 1 | 2 | 1 | 1 | – | – | 1 | – | – | 7 |
| | 1 | 1 | 2 | 1 | 1 | – | – | 1 | – | – | 7 |
| *Funding gap* | *10* | *4* | *4* | *–* | *3* | *1* | *4* | *1* | *3* | *101* | *131* |

### Assumptions for solid waste services (garbage collection and disposal)

- It is assumed there will be an increase in the solid waste fee in 2007 to allow the renewal category to be fully funded. This funding base will be maintained over the next nine years. As a result, costs identified in 2008 will be deferred and funded in future years.
- The strategic initiatives category has not been funded. Council will deal with these initiatives as part of the City Corporate Planning process. If projects in this category are selected for advancement, the garbage fee will be adjusted accordingly.

# TEN-YEAR FORECAST OF NEEDS AND REVENUES – ALL OTHER TAX-SUPPORTED SERVICES

The last category of capital needs is for all other tax-supported services and includes roads, bridges, sidewalks, street lights, City facilities, community and recreation facilities, parks, computers and communication technology, vehicles and equipment.

### Assumptions for all other tax-supported projects

The assumptions built into this portion are as follows:

- The growth category has been funded first because the City has a legal obligation to fund its share of growth projects; Council also set this as the first priority in LRFP II.
- Interest earnings from the Ottawa Hydro endowment fund are assumed to be $13 million for each of the years 2007 to 2016.
- Ottawa Hydro dividends available for capital purposes, net of the annual $12 million transfer to the operating fund, are assumed to be $2 million in 2007, $7 million in 2008, $6 million in 2009, and $7 million for each of the remaining years 2010 to 2016. Actual dividends will be subject to the financial performance of Ottawa Hydro.
- Tax-supported debt is assumed to be $40 million every year, which represents the value of the "revolving debt" that is retired and reissued every year. The revolving debt limits have been shared between transit and all other tax-supported services.
- Forecast development charge revenues are based on average revenues collected over the past two to five years. Any changes, increases or decreases to projected revenues will affect the timing of the identified infrastructure projects. Identified growth needs are in accordance with the development charge funding policy that City Council approved May 24, 2006.
- It is assumed that growth-related projects identified in 2010 and later (beyond the current term of the Development Charge By-law) that are eligible for development charge funding will be included in subsequent terms of the By-law.
- It is also assumed that interest costs will be incorporated in the rates of future development charge by-laws and that debt repayment on current-term projects will also be included in the next term of the By-law.
- Revenues and subsidies from other levels of government, totalling $119 million over the 10-year period, have been included for a number of projects. Consistent with past practice, if these revenues or subsidies are not secured at the time of project approval, the project will either be deferred or project spending will occur only when the revenues are secured.

## Ten-year forecast of needs and revenues – Other tax-supported ($ millions)

| | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Renewal** | | | | | | | | | | | |
| Needs | 218 | 245 | 194 | 214 | 192 | 199 | 188 | 203 | 189 | 173 | 2,015 |
| Funding | | | | | | | | | | | |
| Development charges | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 10 |
| Contribution to capital | 87 | 81 | 80 | 81 | 80 | 81 | 82 | 83 | 79 | 78 | 812 |
| Revolving debt | 28 | 26 | - | - | 31 | 36 | 28 | - | - | - | 149 |
| | 116 | 108 | 81 | 82 | 112 | 118 | 111 | 84 | 80 | 79 | 971 |
| *Funding gap* | *102* | *137* | *113* | *132* | *80* | *81* | *77* | *119* | *109* | *94* | *1,044* |
| **Growth** | | | | | | | | | | | |
| Needs | 129 | 54 | 45 | 79 | 42 | 78 | 56 | 53 | 61 | 92 | 689 |
| Funding | | | | | | | | | | | |
| Development charges | 115 | 46 | 37 | 63 | 35 | 73 | 51 | 47 | 53 | 84 | 604 |
| Contribution to capital | 2 | 2 | 2 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 14 |
| Revolving debt | 12 | 6 | 6 | 15 | 5 | 4 | 4 | 5 | 7 | 7 | 71 |
| | 129 | 54 | 45 | 79 | 42 | 78 | 56 | 53 | 61 | 92 | 689 |
| *Funding gap* | – | – | – | – | – | – | – | – | – | – | – |
| **Strategic initiatives** | | | | | | | | | | | |
| Needs | | | | | | | | | | | |
| City Corporate Plan | 110 | 93 | 80 | 111 | 72 | 89 | 61 | 41 | 64 | 58 | 779 |
| Housing | 20 | 10 | 18 | 11 | 11 | 11 | 11 | 2 | 2 | 2 | 98 |
| Libraries | 1 | 1 | 1 | 1 | 20 | 136 | 1 | 1 | 1 | 1 | 164 |
| Regulatory | 5 | 5 | 4 | 4 | 3 | 3 | 3 | 3 | 2 | 2 | 34 |
| | 136 | 109 | 103 | 127 | 106 | 239 | 76 | 47 | 69 | 63 | 1,075 |
| Funding | | | | | | | | | | | |
| Revenues | 31 | 12 | 12 | 13 | 11 | 12 | 12 | 6 | 5 | 5 | 119 |
| Development charges | 1 | 8 | 2 | - | - | - | - | - | - | - | 11 |
| Contribution to capital/ | | | | | | | | | | | |
| Dedicated funding sources | 10 | 8 | 11 | 5 | 6 | 3 | 4 | 3 | 4 | 2 | 56 |
| | 42 | 28 | 25 | 18 | 17 | 15 | 16 | 9 | 9 | 7 | 186 |
| Funding Gap | | | | | | | | | | | |
| City Corporate Plan | 93 | 78 | 66 | 103 | 64 | 83 | 54 | 35 | 57 | 53 | 686 |
| Housing | - | 2 | 11 | 5 | 5 | 5 | 5 | 2 | 2 | 2 | 39 |
| Libraries | 1 | 1 | 1 | 1 | 20 | 136 | 1 | 1 | 1 | 1 | 164 |
| | 94 | 81 | 78 | 109 | 89 | 224 | 60 | 38 | 60 | 56 | 889 |
| **All categories** | | | | | | | | | | | |
| Needs | 483 | 408 | 342 | 420 | 340 | 516 | 320 | 303 | 319 | 328 | 3,779 |
| Funding | | | | | | | | | | | |
| Revenues | 31 | 12 | 12 | 13 | 11 | 12 | 12 | 6 | 5 | 5 | 119 |
| Development charges | 117 | 55 | 40 | 64 | 36 | 74 | 52 | 48 | 54 | 85 | 625 |
| Contribution to capital/ | | | | | | | | | | | |
| Dedicated funding sources | 99 | 91 | 93 | 87 | 88 | 85 | 87 | 87 | 84 | 81 | 882 |
| Revolving debt | 40 | 32 | 6 | 15 | 36 | 40 | 32 | 5 | 7 | 7 | 220 |
| | 287 | 190 | 151 | 179 | 171 | 211 | 183 | 146 | 150 | 178 | 1,846 |
| *Funding gap* | *196* | *218* | *191* | *241* | *169* | *305* | *137* | *157* | *169* | *150* | *1,933* |

- It is also assumed that revenues and subsidies from other levels of government as identified in the Development Charge Background Study will be forthcoming. There will be an increased cost to the City if these revenues are not realized as identified. This may require projects to be deferred until the required funding is in place.
- As per Council direction, the minimum reserve fund balances for all tax-supported reserve funds, including the transit reserve fund, is $50 million. The forecast assumes that the opening balances are at the minimum level required. Any reduction in the opening balance will result in that year's capital program being constrained to return to the approved minimum balances. In order to fund as much capital as possible, there will be no balance in the city-wide reserve.
- As approved by Council, contributions to capital have been increased by the Infrastructure Construction Price Index (5.1%) in 2007 and remain constant for the full 10-year period. Capital expenditures over the 10 years are also in constant dollars.

## SUMMARY

The funding gap from the re-stated LRFP II to LRFP III has increased by $683 million. The difference is attributable to the increase of $539 million in the net City tax-supported capital requirement and a decrease of $144 million in revenue assumptions.

| | LRFP II Re-stated to reflect changes ($ millions) | LRFP III ($ millions) |
|---|---|---|
| **Gross City tax-supported capital requirement** | **7,494** | **6,752** |
| Less: | | |
| • Revenues | 1,708 | 1,353 |
| • Development charges | 1,848 | 922 |
| **Net City tax-supported capital requirement** | **3,938** | **4,477** |
| Less: | | |
| • Contributions to capital from taxation | 1,102 | 1,048 |
| • Revolving debt | 400 | 400 |
| • GST rebate | 0 | 0 |
| • Hydro dividends | 50 | 64 |
| • Hydro endowment fund interest | 117 | 130 |
| • Provincial gas tax | 284 | 302 |
| • Federal gas tax | 415 | 468 |
| • Gas tax-supported debt | 365 | 239 |
| • Debt servicing from gas tax | (196) | (258) |
| **Total needs not met (funding gap)** | **1,401** | **2,084** |

*Options to reduce the capital funding gap*

The funding gaps vary by category of capital and by available funding sources. The following table shows that while funding gaps exist in the renewal of assets and strategic initiatives category, there is no gap in renewal for transit or solid waste.

| Category | Capital needs ($ millions) | Funding available ($ millions) | Funding gap ($ millions) |
|---|---|---|---|
| Transit renewal | 659 | 659 | – |
| Solid waste renewal | 7 | 7 | – |
| All other – renewal | 2,015 | 971 | 1,044 |
| **TOTAL renewal** | **2,681** | **1,637** | **1,044** |
| Transit growth | 2,120 | 2,120 | – |
| All other – growth | 689 | 689 | – |
| **TOTAL growth** | **2,809** | **2,809** | **–** |
| Transit strategic initiatives | 56 | 36 | 20 |
| Solid waste strategic initiatives | 131 | 0 | 131 |
| All other – strategic initiatives | 1,075 | 186 | 889 |
| **TOTAL strategic initiatives** | **1,262** | **222** | **1,040** |

## Options to address the renewal funding gap

Council has approved a debt strategy where progressively less debt is being applied to the renewal of City assets category of capital. Therefore, the only option to address the funding gap in the renewal of City assets category is to increase the contribution to capital for renewal of City assets from increased taxation.

This option has a direct impact on total taxation. Revenues would be contributed towards requirements identified in the renewal of City assets category, as this category has a higher priority than the strategic initiatives category. A 1% increase in taxation will increase the capital contribution by $9.5 million. A yearly increase of $9.5 million in the contribution to capital would reduce the funding gap by $522 million over the 10-year timeframe.

## Options to address the strategic initiatives funding gap

Options to address the funding gap in the strategic initiatives category of capital are as follows:

**1) Reduce spending in the strategic initiatives category**

Council has heavily scrutinized the strategic initiatives category in the past. However, there are growing pressures from the community to undertake projects in this category that respond to needs resulting from changing demographics.

Changes in the development charge legislation have caused this category of capital to increase, as certain service areas are no longer eligible for funding through development charges. Constraining this category will also limit the achievement of initiatives that implement master plans, acquire environmental areas, and advance the City Corporate Plan. The projects identified as strategic initiatives (excluding regulatory projects) total $1,228 million over the 10-year period, $73 million of which has been funded from dedicated sources like cash-in-lieu, housing reserve, development charges, and some gas tax revenue.

When Council sets its priorities in the City Corporate Plan, it can choose whether or not to proceed with capital strategic initiatives.

### 2) Increase the amount of debt funded from taxes

LRFP III maintains the City policy regarding debt. Debt supported by taxes will be limited to what can be accommodated by the debt servicing envelope. As approved by Council in LRFP II, all other new debt will be funded from gas tax revenues or other non-tax sources. In total, $239 million of non tax-supported debt has been identified as required over the next 10 years.

Of the shortfall identified in the strategic initiatives category, more than $400 million in the 10-year period is eligible for debt financing. Increasing annual debt levels by $9.5 million per year would reduce the funding gap by $95 million, but would require that debt servicing of $31 million be paid from increased taxation over the same 10-year period.

The City's debt is approximately one-third of the level the Province has set as its debt limit. While the total value of debt financing must be managed in order to maintain the City's credit rating, modest increases to the amount of tax-supported debt are presented as an option because the debt enables more capital projects to be achieved within the 10-year timeframe. As the change in the total debt forecast to be authorized has decreased significantly since LRFP II, the risk of having the credit rating reduced is diminished. Council will consider the options identified above as it sets the guidelines for drafting the 2007 to 2010 budgets.


# RATE-SUPPORTED PROGRAMS (WATER AND SEWER)

The City's water and sewer operations are funded through a cost-recovery charge paid by residents and businesses who receive the services from the City. The charge pays for water consumed and discharged into the city's sewer systems. Rural residents who do not have access to municipal water or sewer services are not charged.

This section identifies the financial challenges the City faces in its water and sewer programs. It provides a 10-year forecast of capital requirements, along with a four-year forecast of additional funding requirements to operate the system.

The additional revenues generated from the rate increases outlined in LRFP II are insufficient to fund the operating and capital funding requirements over the 2006 to 2017 time period and to allow for the maintenance of a yearly $20 million reserve fund balance per Council direction. Strategies to address the funding gap are presented in this section.

## OVERALL CAPITAL AND OPERATIONAL NEEDS

The City operates one of the largest and most intricate water and wastewater systems in the province. The City relies on a complex, interconnected network of two water purification plants (WPPs), 14 pumping stations, seven reservoirs, and approximately 2,650 kilometres of water distribution pipes to deliver drinking water to 700,000 customers.

In addition, the City operates and maintains approximately 2,450 kilometres of sewage collection pipes, 81 lift stations and one wastewater treatment facility. On average, 420 million litres of wastewater are treated on a daily basis.

The City has approximately 2,000 kilometres of storm sewers, 14 storm water pumping stations, and 175 storm water management facilities.

The costs associated with operating and maintaining the existing infrastructure are funded primarily from revenues generated from the water and sewer utility bill. The following table provides a summary of 2005 revenues and expenditures.

| | Water ($ millions) | Sewer ($ millions) |
|---|---|---|
| **Revenues** | | |
| • Water and sewer billing | 62.6 | 98.9 |
| • Fire supply/service connection charges | 10.8 | – |
| • Investments and operating revenue | 6.7 | 9.7 |
| | 80.1 | 108.6 |
| **Expenditures** | | |
| • Operating programs | 33.2 | 32.6 |
| • Contributions to capital | 31.1 | 36.9 |
| • Fiscal charges/debt | 1.1 | 13.5 |
| • Cost allocation | 14.7 | 25.6 |
| | 80.1 | 108.6 |

## FUNDING SOURCES

Funding sources for capital, operating, and maintenance costs for water and sewer systems include:

- Water bill revenues – per cubic meter rate charged on water consumption
- Sewer surcharge revenues – percentage rate charged on the amount of water consumed and billed
- Water service charge (replaces former fire hydrant charge) – based on the size of the water meter, this charge contributes to the funding of the infrastructure costs needed to ensure adequate water supply to properties in the event of a fire
- Development charges – revenues generated from the rates applied to new residential/commercial units. These charges provide funding for the growth portion of associated capital projects as identified in the Development Charges By-law and Development Charges Background Study.
- Water and sewer reserves – funds transferred from operations to reserves that enable capital requirements to be funded on a cash basis
- Debt financing – financing source to fund major capital infrastructure

## FOUR-YEAR OPERATING FORECAST

The 2007-2010 operating forecast for rate-supported programs provides Council and rate payers with a high-level overview of estimated expenditures and anticipated revenues over the next four years, based on the best available information. These estimates will be further refined and adjusted during the upcoming weeks as staff develops detailed budget requirements.

### Budget pressure categories

Each year, there are increased cost pressures to deliver water and sewer services to residents. The cost pressures fall into four categories:

**Maintain existing services –** these are the additional resource requirements to continue delivering water and sewer programs and services at the current level of service. In 2005 and 2006, the cost of maintaining services added $5.8 million and $7.3 million respectively to the water and wastewater budgets. Increased user fees have partially offset some cost increases.

**Provincial/legislated –** these are the additional resource requirements resulting from provincial legislation or regulations that:

- Increase the cost of providing existing programs and services at current service levels
- Result in the implementation of a new program, or
- Enhance the service level of an existing program or services

In 2005 and 2006, budget pressures were $150,000 and $439,000 respectively for provincially mandated changes. In 2005, a Ministry of the Environment review required two new laboratory employees to perform additional water and wastewater tests. In 2006, a winter crew was added to comply with new Ontario regulations for disinfection of watermains and the implementation of new licensing requirements for testing and inspection of the water system.

**Growth –** these are the additional resources required to address annual population growth and to service new infrastructure and equipment in new developments. In the last two years, growth-related costs have added $357,000 and $1.53 million respectively to the water and wastewater programs.

**Enhancements –** these are the additional resources required to provide new programs and services to rate payers or to provide a higher level of service for existing Council-approved programs and services. In 2006, $123,000 was added to rate-supported programs, including $35,000 for a Watertrax Water Quality Database, and $85,000 to fund one staff in Infrastructure Services for flood control.

The following table summarizes the annual estimated operating budget pressures identified for the period of 2007 to 2010.

| | 2007 $ thousands | 2008 $ thousands | 2009 $ thousands | 2010 $ thousands |
|---|---|---|---|---|
| **Water Services** | | | | |
| Maintain existing services | 2,740 | 2,607 | 2,295 | 2,467 |
| Provincial/legislated | 112 | 3,164 | 0 | 960 |
| Growth | 374 | 530 | 1,812 | 364 |
| Enhancements | 425 | 170 | 0 | 0 |
| Fees and charges | (338) | (39) | (40) | (41) |
| **TOTAL WATER** | **3,313** | **6,432** | **4,067** | **3,750** |
| **Sewer Services** | | | | |
| Maintain existing services | 1,116 | 1,493 | 1,621 | 1,695 |
| Provincial/legislated | 0 | 0 | 200 | 0 |
| Growth | 440 | 992 | 2,015 | 227 |
| Enhancements | 551 | 0 | 0 | 0 |
| Fees and charges | (120) | (2,820) | (201) | (203) |
| **TOTAL SEWER** | **1,987** | **(335)** | **3,635** | **1,719** |
| **TOTAL COMBINED** | **5,300** | **6,097** | **7,702** | **5,469** |

## Assumptions

The estimates above were prepared using the following assumptions:

- The maintain existing services category includes costs to provide all programs and services at current levels
- Compensation increases were based on bargaining mandates in addition to forecasted cost-of-salary increments and corresponding cost increases to employee benefits
- Inflation on energy costs was assumed to be approximately 7% per year
- Inflation on other materials, supplies and contracted services for 2007 was based on available information, and 2% increases for the subsequent 2008-2010 time period
- User fee increases were set to maintain the cost-to-revenue relationship, along with an increase to the sewer discharge/disposal fees as per the Hauled Liquid Waste Strategy approved by Council
- Impact of commissioning the new waste management facilities at Lemieux and Britannia WPPs (cost to water operations and offsetting recovery of costs in the sewer operations) for:
  - Discharge of water production waste to be treated at the Robert O. Pickard Environmental Centre (ROPEC)
  - Additional disposal costs due to the increased volume of biosolids at ROPEC
- City's participation in the Ontario One-call Consortium was included due to anticipated provincial legislation in 2010
- The commissioning of a new biosolids processing facility at the Robert O. Pickard Environmental Centre in 2009 is included, pending Council approval of a proposed new processing technology
- System growth as new infrastructure is added to water and wastewater systems

### Cost allocation policy review

The City has a cost allocation policy whereby program costs incurred by other City departments in support of the water and sewer function are charged to the water and sewer bill. The policy is intended to allocate an equitable portion of program costs that would otherwise be paid for by property taxes, to the utility rate payer. The allocation of costs to the water and sewer operations is a legacy policy from the former regional government. It was designed to recover the portion of service costs that support the utility operations, in either a direct or indirect fashion.

The cost allocation policy is based on a principle of tax fairness; rural residents who do not benefit from City water and sewer services would pay for these services through their property tax bill in the absence of an allocation. The city-wide tax rate — the primary tax rate levied in the rural areas — would be higher in the absence of this cost allocation.

As part of the 2007 budget process, the current cost allocation will be reviewed to determine if it is at an appropriate level. An analysis will be conducted to examine the types of costs paid through the current cost allocation and will be provided for Council consideration when setting the 2007 budget.

## RATE-SUPPORTED 10-YEAR CAPITAL FORECAST

LRFP III identifies the City's estimated capital requirements for rate-supported projects from 2007 to 2016. Similar to LRFP II, capital requirements have been grouped into three distinct categories that allow Council to prioritize funding as they did in LRFP II. Each category has different funding available for different kinds of projects. Strategies to address funding gaps may vary between categories. The categories are:

1) **Renewal of City assets –** This category reflects the funding required to maintain and/or replace existing capital assets throughout the full life of those assets. Assets include buildings, plants, pumping stations, underground pipes, vehicles, and equipment.

2) **Growth –** This category includes projects that have been identified in the Development Charges Background Study and that align with the goals contained in the City's Official Plan. More specifically, growth projects must have a development charge component that is greater than 30% of the total authority requested. This means developers must pay at least 30% of the cost of the project for it to be considered a capital growth project. Projects where the development charge component is 30% or less are usually categorized as renewal of City assets or strategic initiatives.

**3) Strategic initiatives –** This category includes Council-directed initiatives identified in the City Corporate Plan. Strategic initiatives include projects that:

- Implement the various City master plans and the Ottawa 20/20 plan
- Acquire environmental areas, or
- Enhance services currently being provided to residents

Also included in this category are management initiatives to enhance organizational effectiveness, implement new legislative requirements, and respond to changes in demand for service.

A summary of the capital needs for the 10-year period (2007-2016) is presented in the table below:

| **Category** | **Gross ($ millions)** | | **Net ($ millions)** | | **Total net requirements ($ millions)** |
|---|---|---|---|---|---|
| | **Water** | **Sewer** | **Water** | **Sewer** | |
| Renewal of water and sewer assets | 608 | 652 | 607 | 648 | 1,255 |
| Regulatory requirements | 48 | 6 | 48 | 2 | 50 |
| Growth | 93 | 215 | 32 | 15 | 47 |
| Strategic initiatives | 73 | 169 | 71 | 158 | 229 |
| **Total capital requirements** | **822** | **1,042** | **758** | **823** | **1,581** |

LRFP II had identified a total net requirement of $1,420 million for the next 10 years, which is less than the net requirement in LRFP III.

Total increases in the capital need between LRFP II and III are $161 million. Changes within each category of capital are shown in the table and are followed by explanations.

| **Category** | **10-year net requirements ($ millions)** | | |
|---|---|---|---|
| | **LRFP II** | **LRFP III** | **Change** |
| Renewal of water and sewer assets | 1,004 | 1,255 | 251 |
| Regulatory requirements | 159 | 50 | (109) |
| Growth | 101 | 47 | (54) |
| Strategic initiatives | 156 | 219 | 73 |
| **TOTAL** | **1,420** | **1,581** | **161** |

*Inflation in the construction industry*

LRFP II cost projections were prepared in early 2004 and reflected prices known at that time. LRFP III has projected costs in 2006 dollars. As outlined in the previous section of this document, the City's construction industry has been subjected to significant price increases. Most rehabilitation projects have increased from between 5% and 10% as a result of significant inflationary cost increases for energy and construction materials such as steel, asphalt, and concrete.

## NEW INITIATIVES AND INFORMATION ON INFRASTRUCTURE CONDITION

Reductions in the provincial/legislated and growth budget pressure categories are due mainly to significant projects included in LRFP II that have been either reduced, or are not included in LRFP III, such as the Combined Sewer Area Management Program for $79 million. Projects that have been completed, or are near completion and as a result do not have additional funding requirements in the 2007-2010 time period, include:

- Water Purification Plant Waste Management Project ($27 million)
- ROPEC Plant Expansion ($24.5 million)
- North Kanata Sewer and Pumping Stations ($19 million)

Programs such as the Service Connection Rehabilitation Program for sewer repairs have increased to $55 million in the renewal of City assets category. Other projects such as Sandy Hill flood relief ($16.5 million) and ROPEC major plant upgrades ($9.5 million) have moved from the strategic initiatives category to the renewal category to reflect the ongoing nature of the programs.

### Advanced lead service replacement program

On July 11, 2006, Council approved a proactive Lead Service Replacement Program with an annual cost of $1 million. Staff has been directed by Council, through Motion Number 62/25, to "provide, for the 2007 budget a strategy to replace the City's portion of lead water services by 2012."

No estimates have been provided or included in the forecasts for this project in LRFP III. Staff is currently preparing a detailed plan on the impact this enhancement will have on taxes and rates. As per Council's direction, this plan will be brought forward as part of 2007 budget deliberations.

*New provincial regulations – Clean Water Act and Sustainable Water and Sewage Systems Act*

The water and wastewater industries are in the midst of an unprecedented period of regulatory change. The Province is developing regulations based on their established conceptual framework. The impact of these two acts on operations and associated costs are unknown at this time. Staff has anticipated that the regulations would be made public in late 2006. As of print time, no information had been released by the Province. Once this information is known, staff will evaluate the regulations and report to Council with a detailed plan to identify potential incremental costs, changes to operations, and impacts on the rate structure.

## CURRENT RATE-SUPPORTED FUNDING GAP

When current capital funds are applied to the 10-year capital requirements, there are funding gaps in both the water and sewer capital programs. Available funding contributions to water and sewer capital programs and gaps over the next four years are summarized as follows:

| | 2007 ($ million) | 2008 ($ million) | 2009 ($ million) | 2010 ($ million) | 10-year totals ($ million) |
|---|---|---|---|---|---|
| Combined net capital needs | (183.5) | (187.3) | (176.8) | (137.5) | (1,581.3) |
| New debt | 1.6 | 1.6 | 43.6 | 2.4 | 64.2 |
| Combined capital contribution | 69.4 | 78.7 | 82.6 | 89.8 | 1,086.1 |
| Annual combined gap | (112.5) | (107.0) | (50.6) | (45.3) | (431.0) |
| Cumulative gap | (112.5) | (219.5) | (270.1) | (315.4) | (431.0) |

### Assumptions

The above funding was forecasted using the following assumptions:

- A combined water and sewer surcharge rate increase of 9% in 2007, and 5% annual increases from 2008 to 2016. The increases reflect a water rate increase of 12% for 2007, and 5% in 2008 and beyond, and a sewer surcharge decrease of 4% for 2007 (rate to be maintained to 2016). Use of debt financing for the City's share of growth projects, significant and unique regulatory capital requirements, process modifications, or strategic initiatives.
- A minimum combined water and sewer reserve fund balance of $20 million each year

LRFP II recommended net rate increases that, at the time, were believed to be sufficient to meet the long-term requirements of the operating and capital programs for rate-supported programs. Included in that analysis were assumptions about the volume of water that would be consumed. Revenues generated from rate-supported programs are in direct proportion to the volume of water consumed and billed.

Actual quantities of water billed in 2004 and 2005 were significantly less than the volume estimates prepared for LRFP II. As a result, water and sewer revenues have been lower than projected. The volume differences were previously identified in Unaccounted for Water reports and the more recent Water Tight Report to Committee and Council. Investigations are underway to identify the causes for these volume differences.

The following table identifies variances between LRFP II volume estimates and actual use, and the impact of revenue reductions.

| | 2004 | | | 2005 | | |
|---|---|---|---|---|---|---|
| | LRFP II | Actual | Variance | LRFP II | Actual | Variance |
| Volume of water billed ('000 m3) | 99,700 | 96,691 | (3,009) | 99,949 | 93,809 | (6,149) |
| Water revenues ($ thousands) | 61,824 | 59,036 | (2,788) | 69,021 | 62,612 | (6,409) |
| Sewer surcharge revenues ($ thousands) | 102,628 | 94,108 | (8,520) | 109,657 | 98,872 | (10,785) |
| Total revenues ($ thousands) | | | (11,308) | | | (17,194) |

As consumption volumes are not reaching LRFP II estimates and capital needs have not reduced significantly, rates will need to be adjusted for revenues to cover costs.

The cumulative funding gap of $431 million identified during the 2007-2016 period is highest in the first four years representing $315.4 million. The proposed strategy to address the gap in the first four years and for the remaining years six years is as follows:

## *Options to close funding gap*

- Increase the water rate and decrease the sewer surcharge for a combined net increase of 9% in each year from 2007 to 2010; 5% combined rate increase for 2011 to 2013; and, 2% combined rate increase for 2014 to 2016.
- Defer any strategic initiatives that are not regulatory in nature. Strategic initiatives projects can be considered in future years should additional funding capacity exist.
- Increase the amount of capital work funded by debt.
- Maintain an average balance of $20 million in the reserve funds over the 10-year period rather than the Council policy of a yearly $20 million balance.

The following table details changes to each of the rates and the debt required to be authorized to ensure that 2007 and 2008 capital renewal and growth needs can be met.

| | 2007 | 2008 | 2009 | 2010 |
|---|---|---|---|---|
| Water rate increase | 12% | 16% | 15% | 9% |
| Proposed water rate | $0.868 | $1.007 | $1.158 | $1.263 |
| Sewer surcharge decrease | (4.6%) | (10.3%) | (9.2%) | 0 |
| Proposed surcharge rate | 145% | 130% | 118% | 118% |
| Net impact on water bill | 9% | 9% | 9% | 9% |
| | | | | |
| | $ million | $ million | $ million | $ million |
| Forecast funding gap | (112.5) | (107.0) | (50.6) | (45.3) |
| Increase in contribution to capital reserve funds | - | 7.7 | 6.9 | 7.0 |
| Additional debt | 69.6 | 72.3 | - | - |
| Deferral of strategic initiatives | 31.5 | 59.6 | 25.6 | 15.3 |
| Draw from reserves (Contribution to reserves) | 11.4 | (32.6) | 18.1 | 23.0 |

The proposed rate increases would generate an additional $51.2 million over the next four years and $188.9 million over the 10-year period to offset the shortfall mentioned previously.

Reducing the strategic initiatives capital requirements in the next four years decreases the gap by $132 million. Maximizing debt financing for the renewal portion of the capital program in 2007 and 2008 increases debt by $141.9 million, with the principal and interest repayments to be funded from future revenues. Rate increases will allow for an additional $21.6 million to be contributed to the capital reserve funds with a net drawdown over the four years of $19.9 million. The balance in the capital reserve fund will average approximately $24 million over the 2007 to 2010 period and $29 million over the 10-year period.

# LONG-RANGE FINANCIAL PLAN – ISSUES AND STRATEGIES


LRFP III reflects how Ottawa is not alone in facing constrained funding circumstances or growing pressure to maintain funding for existing programs and services. Changing demographics and a growing population create pressures on the City to provide new programs and services with no readily available source of funding. In short, Canadian municipalities face many challenges as they try to become financially sustainable.

Various issues or themes identified in LRFP III need to be addressed before the City of Ottawa can become financially sustainable. 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.

This section presents a summary of the issues and proposes strategies for Council's consideration as we aim to make the City financially sustainable over the long-term.

## ISSUE 1

### Provincial social programs should not be on the tax bill and the Province is not adequately funding its share of cost-shared programs.

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

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.

As discussed in previous sections, the cost for services mandated by the Province is projected to increase significantly over the forecast period. Preliminary projections for 2007 indicate that rates for Ontario Works, the employment and financial services program, will increase by 2%. Prescription drugs are projected to increase at rates higher than inflation, as will Ontario Disability Support Payments. Per diem rates and operating subsidies in the housing program are also projected to increase at rates higher than originally projected. On an annual basis, the costs for mandated programs are forecast to increase between $6 to $8 million 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.

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 approximately $16 million. Under the current arrangement, there is no other choice than to fund the gap from Ottawa property taxes. The City is mandated to provide these programs at the level of service determined by the Province.

Strategies to reduce the impact of provincial social programs on property taxes or to have them removed from 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.
- 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.

## ISSUE 2

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

The grants and subsidies from the Province and other municipalities that Toronto receives 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.

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 benefit from 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 Province has recognized that social service costs are causing significant budget pressure in many municipalities, and has recently revised the Ontario Municipal Partnership Fund (OMPF). Contrary to how municipal funds are raised (based on assessment), the OMPF will provide grants to municipalities with high social costs that are relative to the household income levels of its residents. This formula ignores the fact that commercial properties also contribute towards social service costs. While Ottawa has a smaller commercial base than Toronto, it has higher household income. Ottawa will receive $6 million from the OMPF, 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 Toronto's residents, Ottawa's grant would be $12 million.

The issue of Ottawa receiving its fair share of grant programs is related to the strategy of having provincial expenditures removed from the local municipal tax bill. The City's position is that funding for social services should be part of provincial income taxation. That way, funding would be based on the principle of "ability to pay" rather than property ownership.

Strategies to remove inequities in provincial grant allocations:

- 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.

## ISSUE 3

### Ottawa taxes are similar to other large Ontario cities.

Ottawa taxes have increased by an average of 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. This is largely due to Ontario being the highest property tax jurisdiction in the country as a result of social program funding requirements on the property tax bill.

Ottawa has recently been faced with many challenges as a result of the provincial property tax system. Taxpayers have been frustrated by changes in their property assessment and resulting tax increases. Tax shifts have been misinterpreted as budgetary tax increases and Ottawa City Council has had to implement emergency programs to mitigate the negative impacts of these shifts. To allow Council to focus on its priorities rather than the impacts of re-assessment, the property tax system has to be fixed.

While Ottawa's taxes are not the highest in the Province, comparisons are often made between the residential taxes paid in Ottawa and those paid in Toronto. Because the real estate markets in each city are different, the use of a single assessment value for tax comparison purposes is misleading. For example, in Toronto the average home is valued at $369,000 compared to an average home in Ottawa at $276,245. An average homeowner in Toronto paid $455 less in taxes in 2006 than an average homeowner in Ottawa. That is only part of the story.

Commercial properties in Ottawa make up 14% of the assessment base but pay 26% of the taxes, or 1.85 times their value. Toronto's commercial properties make up 17% of the assessment base, but pay 37% of the taxes or 2.18 times their value. As commercial properties are paying a larger share of total taxes in Toronto, the residential sector does not have to pay as much.

The Province requires that tax increases resulting from assessment changes in the commercial classes be phased in through the use of a tax cap. This means that some properties have tax increases limited because of the cap. Other properties not under the cap end up subsidizing capped properties. Since 1998, the tax cap has resulted in mainly small Ottawa commercial properties paying more tax to provide tax relief to larger commercial properties. The objective of tax predictability has been achieved at the expense of tax fairness.

Another inequity built into the current tax system is the way the education tax rate is calculated for residential properties. The Province calculates the rate using all of the residential property assessment values in Ontario. Ottawa's residential property assessment increases have been above the provincial average. As a result, Ottawa residents are paying a larger share of education taxes than they should. Since 2001, Ottawa residents have paid $28 million more in education property taxes.

There are many other tax policy issues that must be addressed to ensure the property tax system is equitable and explainable. The Province has just announced a two year freeze on assessments to deal with the results of the Ombudsman's report on problems with the Municipal Property Assessment Corporation. This will give the City a short reprieve from the issues that stem from re-assessment. However, unless changes are made to existing tax policy, or Councils are allowed more tools and discretion in the application of tax policy, the issues will not go away.

Strategies to 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.

## ISSUE 4

**The City's operating spending is in line with other Ontario cities, but costs are rising above the Consumer Price Index.**

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 more than $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, but 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 due to harsher winters and the larger geographic size of the City. In addition, 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.

Based on the best information currently available, it is projected that the cost increases to maintain existing City services will range from $55 to $61 million on an annual basis.

Strategies to control costs and reduce consumption:

- Maintain existing service levels and 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 implement conservation and reduction guidelines and policies that minimize the amount of goods used.
- Maintain appropriate operating reserves for programs with expenditures that can vary significantly from year to year to smooth the budgetary impact.

## ISSUE 5

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

Approximately 95% of the City's workforce is unionized. 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.

Strategies to better manage compensation costs:

- 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.

## ISSUE 6

### Changing demographics mean changing municipal service needs.

Ottawa's population is growing and the demographic profile is changing. As a result, there is pressure on the City to respond with expanded services or infrastructure and programs that reflect the demographic make-up of the City.

The City has limited sources of funding to respond to these pressures. Therefore, it is paramount that Council prioritize the issues it would like addressed in the short-term. The City Corporate Planning process has been established for this purpose and will be used to allocate any funding available for these new or enhanced services.

One of the main sources of revenue from which the City can fund new infrastructure is the Development Charge legislation. However, there are a number of changes needed to this legislation before growth can truly pay for itself.

A list of strategies available to assist in addressing the impacts of a growing and aging population follows.

Strategies to 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 initiatives 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.

## ISSUE 7

### Cities need new revenue sources other than taxation.

There are only three funding tools available to cities that they can control: property taxes, user fees, and development charges. It would require increases well above inflation for these three funding tools to meet the annual growth in City of Ottawa expenditures. Ottawa is already more dependent on property taxation than other Ontario municipalities because it does not receive the same level of assistance for its social programs. Ontario municipalities have the most limited access to other forms of non-taxation revenue in Canada, but pay a greater share of provincial programs.

Recognizing the limitations on property tax increases, the City of Ottawa has adopted a user pay approach since amalgamation to fund a portion of program or service costs. Ottawa adopted a policy that ensures user fees increase with the cost of providing a service so that tax subsidies do not increase. The City also created a target for transit fare revenues to pay a higher percentage of operating costs. Garbage collection and disposal are also paid through user fees.

However, the City must look beyond taxation and user fees to other sources of revenue if it is to become financially sustainable.

Strategies to increase revenues:

- Increase 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.

## ISSUE 8

### 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."[42]

Recent studies attempting to measure the infrastructure gap in Canada show that it is still significant and must be addressed if Canada is to remain internationally competitive. Ontario municipalities are responsible for the largest share of public infrastructure in Canada and the needs in this province are the greatest.

[42] Standard and Poors, Public Finance Report Card: Municipalities. May 25, 2006.

Ottawa is an older city (some infrastructure is more than 100 years old) and it is continuing to grow. Projects providing proper maintenance of existing City assets compete for funding with projects to add new assets such as roads and sewers. Other capital projects responding to demographic changes or Council priorities are also required. As a result, sources of revenue for capital projects are not sufficient to meet the needs in all three areas.

LRFP I successfully framed the debate around the need for sustainable sources of funding from other levels of government to bridge the City's infrastructure gap. The provincial gas tax and the federal gas tax are welcome funding for municipalities, but they have very limited application. The City would like to be able to progress on all its capital needs, not just those associated with transit. The current funding rules do not allow this.

The capital program as presented in LRFP III identifies a $6.7 billion requirement over the next 10 years to address the renewal of existing infrastructure, growth requirements, and strategic initiative projects in support of the City's Corporate Plan. Based on the funding sources currently available to the City, a "funding gap" of approximately $2.1 billion is projected. Of this gap, $1.1 billion of the projected shortfall would address renewal requirements funded from taxation. The remaining $1 billion of the shortfall would fund strategic initiatives projects.

While there may be sources of funds to build new assets (primarily development charges), once they are built they must be maintained and repaired, or may require staff to operate. This causes pressure on the operating budget, which in turn causes pressure to defer maintenance in order to avoid a large tax increase.

Increasing contributions to capital from taxes competes with the desire to keep taxation increases below the rate of inflation. The City uses debt to fund some of its infrastructure needs, but this source of funding is limited to projects funded from non-taxation sources of revenue. As a result, debt repayment, as a percentage of the total tax bill, has declined since amalgamation.

Strategies to ensure infrastructure projects are adequately funded:

- Increase contributions to the capital budget at the rate of increase in the 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.

## ISSUE 9

**Liabilities that are incurred today must start to be funded by today's taxpayers.**

One of the measures of financial sustainability is that future generations are not forced to pay for services provided to the current generation. The City incurs expenses that do not have to be paid immediately (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.

Strategies to 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, the post-employment or retirement employee benefits liabilities.

## NEXT STEPS

LRFP III provides information the new Council will need to work with residents in developing 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.

For more information on the City of Ottawa's programs and services, visit
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