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**To:** Finance Committee **Date:** September 19, 2006  
**From:** Andrew Nazareth **File:** 03-0970-01/2006-Vol 01  
General Manager, Business & Financial Services  
**Re:** Long Term Financial Management Strategy Update

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**Staff Recommendation**

That the Long Term Financial Management Strategy update be received for information.

Andrew Nazareth  
General Manager, Business & Financial Services  
(4095)

<b>FOR ORIGINATING DEPARTMENT USE ONLY</b>		
<b>CONCURRENCE OF GENERAL MANAGER</b> 		
<b>REVIEWED BY TAG</b>	YES <input checked="" type="checkbox"/>	NO <input type="checkbox"/>
<b>REVIEWED BY CAO</b>	YES 	NO <input type="checkbox"/>

## Staff Report

### Origin

Pursuant to Council requests for updates with respect to the current financial status of the Long Term Financial Management Strategy.

### Background

In 2003, the Long Term Financial Management Strategy (LTFMS) was adopted to address Richmond's challenges with insufficient revenue sources, ageing infrastructure, provincial downloading, rapid infrastructure expansion associated with urban growth, fluctuating market conditions, decreasing reserves and a lack of control over external costs.

As previously reported, during the mid-1990's, Richmond lost \$5.7 million in provincial grants, and was subject to rising external costs. Richmond chose to absorb the loss of provincial grants and rising costs by reducing contributions to the reserves and finding significant efficiencies in order to require only nominal tax increases to property owners.

As a result, these past strategies had put the City in a tight financial situation. The reserve balances were shrinking and the difference between the actual reserve balance and the estimated required reserve levels was widening.

Council and senior staff realized that something had to change and on May 26, 2002 Council directed staff to develop a Long Term Financial Management Strategy. To this end, the LTFMS model was created to address Richmond's financial challenges. The objective was to enhance the City's economic well-being for future generations as part of the well managed component of the City's vision without sacrificing the components of the City's vision which affects the overall liveability of the community. The ten policies that govern the LTFMS are as follows:

1. Tax Revenue - Tax increases will be at Vancouver's CPI rate (to maintain current programs and maintain existing infrastructure at the same level of service) plus 1.0 % towards infrastructure replacement needs.
2. Gaming Revenue - Gaming revenues will go directly to the capital reserves, the grants program and a community legacy project reserve.
3. Alternative Revenues & Economic Development - Any increases in alternative revenues and economic development beyond all the financial strategy targets can be utilized for increased levels of service or to reduce the tax rate.
4. Changes to Senior Government Service Delivery - Any additional costs imposed on the City as a result of mandatory senior government policy changes should be identified and added to that particular year's taxes above and beyond the CPI and infrastructure percentage contribution.
5. Capital Plan - Ensure that long term capital funding for infrastructure (e.g. parks, trails, facilities, roads etc.) is in place in order to maintain community liveability and generate economic development.
6. Cost Containment - Staff increases should be achieved administratively through existing departmental budgets, and no pre-approvals for additional programs or staff beyond

existing budgets should be given, and that a continuous review be undertaken of the relevancy of the existing operating and capital costs to ensure that the services, programs and projects delivered continue to be the most effective means of achieving the desired outcomes of the City's vision.

7. Efficiencies & Service Level Reductions - Savings due to efficiencies or service level reductions identified in the strategy targets should be transferred to the capital reserves. Any savings due to efficiencies beyond the overall strategy targets can be utilized to reduce the tax rate or for increased levels of service.
8. Land Management - Sufficient proceeds from the sales of City land assets will be used to replenish or re-finance the City's land inventory. Any funds in excess of such proceeds may be used as directed by Council.
9. Administrative - As part of the annual budget process the following shall be undertaken:
  - all user fees will be automatically increased by CPI;
  - the financial model will be used and updated with current information, and
  - the budget will be presented in a manner that will highlight the financial strategy targets and indicate how the budget meets or exceed them.
10. Debt Management - Utilize a "pay as you go" approach rather than borrowing for financing infrastructure replacement.

## **Analysis**

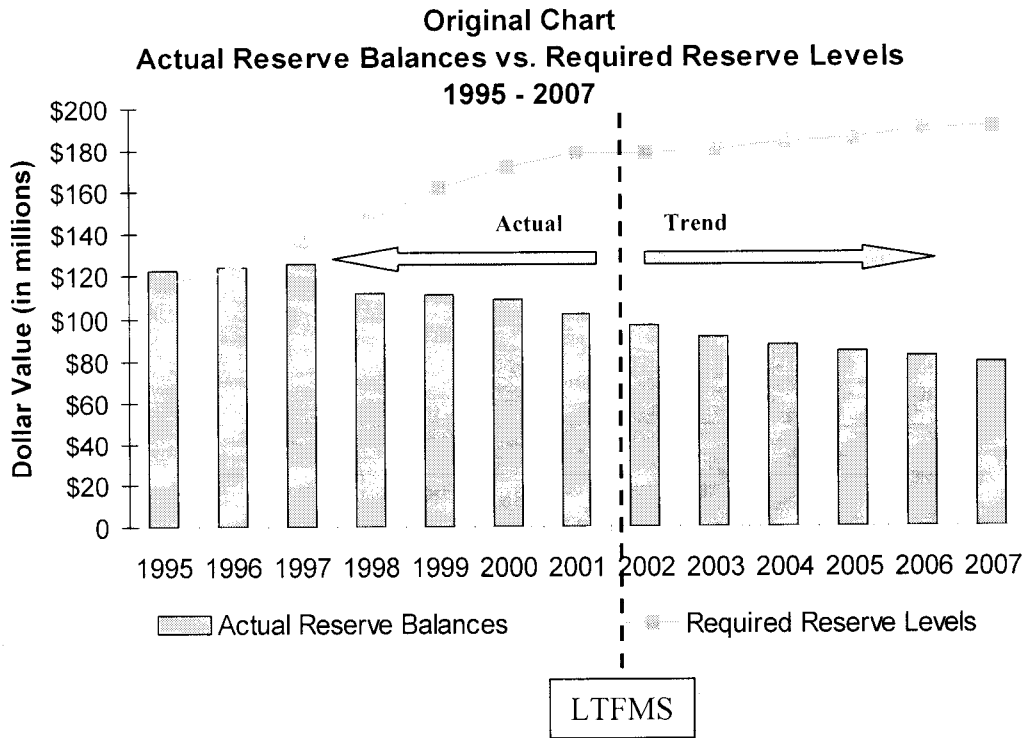
### **Reserve Balances**

Since the inception of the LTFMS, the reserve balances have been growing steadily. The growth can be attributed to a combination of items including:

- The Long Term Financial Management Strategy (LTFMS) adopted by Council
- Significant DCC revenues due to growth
- Increase in Casino revenues
- Increase in transfer to reserves by Council
- Increase in surpluses as a result of Building Permit revenues from increased construction activity and traffic fine revenue.

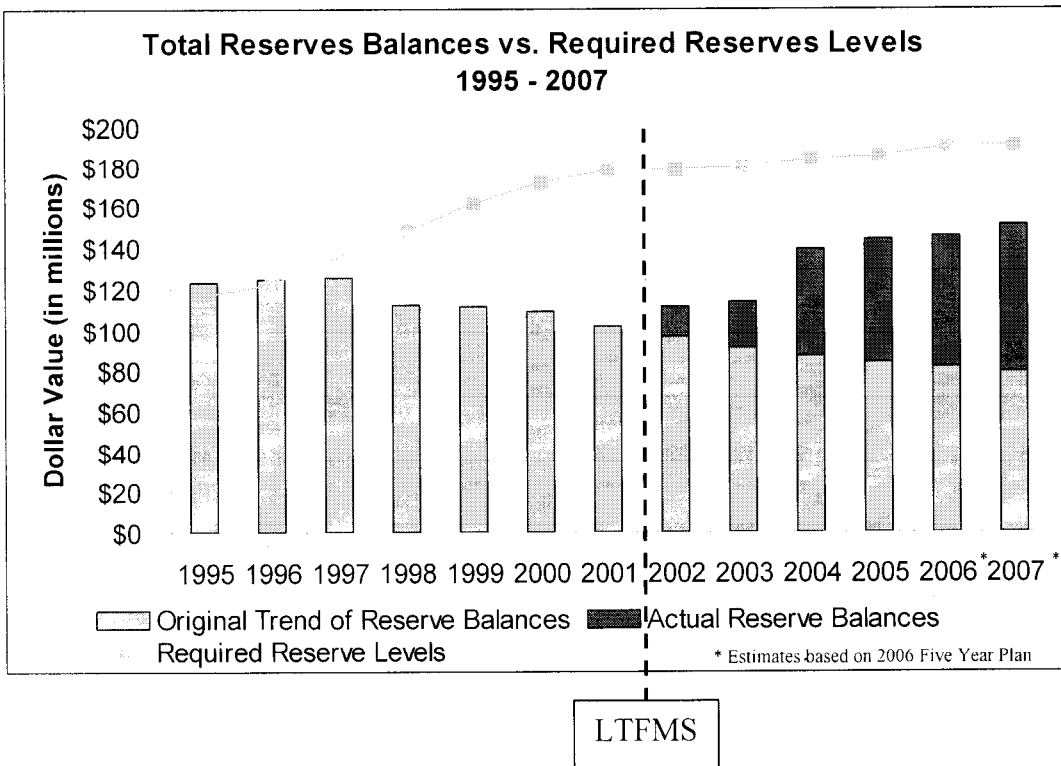
The original reserve chart (Figure 1.) prepared for Council in mid-2002 shows the probable reserve balances if the trends displayed from 1997 – 2001 continued. This chart emphasises the increasing gap between the estimated required levels of reserves and the actual reserve balance.

Figure 1.



Due to the items listed above and other factors, the declining trend of reserve balances was averted. At the end of 2005, the reserves have grown to \$143.6 M from \$102.1M at the end of 2001. Figure 2. shows the actual reserve balances in relation to the projected trends noted in mid 2002.

Figure 2.



## LTFMS Policies

The implementation of the LTFMS in 2003 included ten policies which govern the financial activities of the City. The analysis below summarizes the level of adherence to these policies:

Policy	Analysis	Standing																									
1. Tax Revenue	<table border="1" data-bbox="345 384 1336 569"> <thead> <tr> <th></th> <th>Base Increase</th> <th>Additional Level</th> <th>Reserves</th> <th>Total Increase</th> </tr> </thead> <tbody> <tr> <td>2003</td> <td>2.90%</td> <td>0.45%</td> <td>1.00%</td> <td>4.35%</td> </tr> <tr> <td>2004</td> <td>2.51%</td> <td>0.76%</td> <td>0.47%</td> <td>3.74%</td> </tr> <tr> <td>2005</td> <td>1.25%</td> <td>0.73%</td> <td>0.00%</td> <td>1.98%</td> </tr> <tr> <td>2006</td> <td>2.01%</td> <td>0.97%</td> <td>1.00%</td> <td>3.98%</td> </tr> </tbody> </table> <ul style="list-style-type: none"> <li>- The implementation of the LTFMS was in 2003 and the tax increases from that point in time are keeping within the budgeted CPI increase</li> <li>- The increase to reserves was fully met in 2003 and 2006 with a partial increase in 2004</li> </ul>		Base Increase	Additional Level	Reserves	Total Increase	2003	2.90%	0.45%	1.00%	4.35%	2004	2.51%	0.76%	0.47%	3.74%	2005	1.25%	0.73%	0.00%	1.98%	2006	2.01%	0.97%	1.00%	3.98%	Meets Requirement
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2. Gaming Revenue	<ul style="list-style-type: none"> <li>- Gaming Revenue is currently used to fund capital reserves and the community grants program.</li> </ul>	Meets Requirement																									
3. Alternative Revenues & Economic Development	<ul style="list-style-type: none"> <li>- Additional revenues from alternative revenue sources and economic development need to be developed in order to reduce the overall tax impact.</li> </ul>	Needs Improvement																									
4. Changes to Senior Government Service Delivery	<ul style="list-style-type: none"> <li>- The RCMP and ECOMM contracts have increased at rates greater than the LTFMS policy of CPI. Consideration should be made on whether these are Senior Government items. RCMP increases are highlighted within the annual budget presentations.</li> </ul>	Needs improvement																									
5. Capital Plan	<ul style="list-style-type: none"> <li>- The Five Year Capital Plan is created on a yearly basis and projects the anticipated capital program costs and funding availability.</li> <li>- This ensures that the approved projects have future funds available to finance their costs.</li> </ul>	Meets Requirement																									
6. Cost Containment	<ul style="list-style-type: none"> <li>- On a yearly basis, the budget submissions are reviewed and analyzed.</li> <li>- Increases have been achieved through existing budgets wherever possible.</li> </ul>	Meets Requirement																									
7. Efficiencies & Service Level Reductions	<ul style="list-style-type: none"> <li>- Review of these efficiencies or service level reductions have not been isolated on a year-by-year basis and are generally combined with the remaining operating costs.</li> </ul>	Needs Improvement																									
8. Land Management	<ul style="list-style-type: none"> <li>- The proceeds from land sales are returned to land related accounts to fund future land acquisitions.</li> <li>- There are no specific clauses limiting the use of these funds to only land acquisitions.</li> </ul>	Meets Requirement																									
9. Administrative	<ul style="list-style-type: none"> <li>- Currently where possible user fees are automatically increased by CPI on January 1st of each year.</li> <li>- Every year, the Five Year Plan is prepared and addresses the tax increase, distribution of gaming revenue, isolation of additional levels of service and capital plan funding sources.</li> <li>- The financial model and strategies are considered when decisions are made, but there are also areas of improvement regarding communication of the financial model.</li> </ul>	Needs Improvement																									
10. Debt Management	<ul style="list-style-type: none"> <li>- Since the construction of the No. 2 Road Bridge, no capital project has required debt for financing. This form of efficiency allows for the savings from interest payments that would otherwise be payable.</li> </ul>	Meets Requirement																									

Overall, four out of the ten policies require improvement, specifically; Alternative Revenues & Economic Development, Changes to Senior Government Service Delivery, Efficiencies and Service Level Reductions and Administrative. Staff will continue to update the 20 year model on an ongoing basis in order to monitor progress.

The one policy that may need to be revisited is Policy 1 concerning tax revenue and benchmarking to CPI.

## **CPI**

While the CPI is a good indicator of inflation for households, it is not a good indicator of what municipalities purchase. The municipal basket of goods includes externally purchased services and supplies, operating costs from new infrastructure, collective agreements, RCMP & Fire Rescue services, costs for shared provincial programs as well as asphalt, salt, steel, diesel fuel and electricity. As a result of the differences between CPI and the price increases a municipality will face, some municipalities are developing their own Municipal Price Index (MPI) to track the magnitude of inflation anticipated for their basket of goods.

Using the MPI instead of CPI as the gauge of inflationary increases would better reflect the actual expenses to be incurred by the City. Policy one of the LTFMS requires that the tax increases are limited to CPI plus 1% for transfers to reserves. However, the actual change in costs to the City can be much different than CPI.

Even though the average consumer understands the increases of CPI, the City must forecast based on actual cost increases as represented by MPI. If the tax rate increases are limited to CPI, the potential requirement to fund the gap from surplus might be required.

## **Conclusion**

The LTFMS is currently on track as the reserve balances are increasing and at a rate which will enable the required reserve levels to be reached in a faster timeframe than originally anticipated. This has been done following the majority of policies set out by the LTFMS.

Certain LTFMS policies relating to administration as well as identifying efficiencies have not been implemented to their greatest potential.

The one LTMFS policy relating to the use of CPI as a gauge of inflationary costs may require further review as the measure may not be the most relevant to municipal business.



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