Clarington

# Staff Report

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| **Report To:** | **Joint Committees** | | |
| **Date of Meeting:** | September 13, 2021 | **Report Number:** | FSD-040-21 |
| **Submitted By:** | Trevor Pinn, Director of Financial Services/Treasurer | | |
| **Reviewed By:** | Andrew C. Allison, CAO | **Resolution#:** | |
| **File Number:** | [If applicable, enter File Number] | **By-law Number:** | |
| **Report Subject:** | 2022 Budget Guidelines | | |

## Recommendations:

1. That Report FSD-040-21 and any related communication items, be received;
2. That Staff prepare a draft budget with a target municipal increase of 3.95 per cent;
3. That Staff include within the draft budget requests for funding from external agencies up to a maximum of 3.30 per cent;
4. That the 2022 budget schedule, as outlined within Report FSD-040-21, be approved;
5. That all interested parties listed in Report FSD-040-21 and any delegations be advised of Council's decision.

## Report Overview

Council adopted a budget policy that guides the preparation of the annual operating and capital budgets process. The budget policy requires an annual report to Council to determine the target municipal levy change for the following year. This report meets that policy requirement.

# 1. Background

### Budget Policy

1.1 On June 10, 2019, Council approved a new Budget Policy which provides guidance on the creation and preparation of the annual operating and capital budgets.

1.2 As part of the policy, the Director of Financial Services/Treasurer is required to report to Council in September of each year with a report seeking guidance on the target municipal levy increase for the upcoming budget year. This report meets this policy requirement.

# 2. Economic and External Factors

2.1 The Municipality of Clarington's budget must take into consideration economic factors impacting the Municipality and local region, as well as the broader economic factors impacting all of Ontario and Canada. This section provides highlights on the economic factors impacting the development of the 2022 budget.

### Political Factors

2.2 An external factor which could impact the Municipality are pending political elections. When a change in government occurs there are potential changes in priorities which could impact the Municipality. Grant opportunities could become more favourable leading up to an election or may be stalled during the election process. The methodology of grants, being application or formula based, could also change with a change in government.

2.3 A federal election has been called for September 20, 2021. A significant amount of capital funding that the Municipality receives is through grants involving the Government of Canada, the approval of these pending applications could be impacted or completely cease depending on any changes to the mandate of the Government of Canada (or new Government of Canada).

2.4 The Province of Ontario is due to have an election on or before June 2, 2022. The Province has already passed a resolution indicating that an early election will not occur, given that the current government is a majority-government it is not anticipated that an early election will occur. Municipalities in Ontario are subject to Provincial legislation and receive significant grant opportunities (both operating and capital) through the Province or through a partnership of the Province and Federal government. Similarly, to a change in federal government, a change at the Provincial level could result in changes in funding priorities which have a direct impact on the Municipality.

2.5 Municipal elections are set for October 24, 2022 for all municipalities in the Province of Ontario. As municipal elections in Ontario are not party-based, the impact of a potential change in municipal councils on the Municipality’s budget are harder to predict in the long-term.

**Canadian Economy**

2.6 The Bank of Canada announced in it’s July 2021 Monetary Policy Report, that the target rate of inflation of the consumer price index (CPI) remains at 2 per cent. The target is the midpoint of the 1 to 3 per cent control range that the Bank of Canada has set.

2.7 The Bank of Canada forecasts that economic growth, weak in the first half of 2021, will pick up strongly in the third quarter as the economy reopens. Consumption is expected to lead the rebound with increases in spending on transportation, recreation and the food and accommodation services. The Bank expects the economic recovery to be more broad-based and self-sustaining over the projection period.

2.8 The impact of the pandemic has been uneven on the economy, and a full and inclusive recovery is projected to take time. Broad immunity is assumed to be achieved in the third quarter of 2021 with a corresponding easing of public health restrictions by the end of the third quarter of 2021.

2.9 The Bank of Canada expects CPI to remain elevated throughout the rest of 2021 due to the temporary factors related to the pandemic. As the pandemic factors lessen in the second half of 2021 and into 2022, the Bank of Canada expects CPI to ease to about 2 per cent. This will then increase slightly in 2023 before returning in 2024.

2.10 The labour market is expected to continue to see a strong rebound in employment; however, expected changes in the economy which are more structural may result in some having longer periods of unemployment.

2.11 The Bank of Canada is expecting the Canadian economy to see a CPI increase in 2022 of 2.4 per cent (this is higher than the previous forecast of 1.9 per cent) and 2.2 per cent (this is lower than the previous forecast of 2.3 per cent) in 2023. Real Domestic Product

(RDP), an indicator of economic growth, is expected to be 3.8 per cent in 2022 and 3.1 per cent in 2023.

2.12 TD Economics, in their July Dollars and Sense, is predicting inflation to remain at 4 to 5 per cent through 2021 reducing to 3 per cent by the end of 2021. By the end of 2022, it is expected that inflation will be approximately 2.5 per cent.

2.13 The overnight target rate, currently at 0.25 per cent, is not expected to increase until the fourth quarter of 2023. This will continue to result in a low cost of borrowing, which is advantageous to the Municipality, but also a low interest income market. The interest rate on 10-year government bonds is expected to go from 1.39 per cent at Q2 2021 to 2.25 per cent starting in Q2 2022 and staying stable through the end of the year.

2.14 Overall, the expectation appears to be a hot recovery in the Canadian economy in the latter part of 2021 and into 2022; however, many of the economists assumptions are based on continued vaccination and immunity levels being reached in the third quarter of 2021.

**Ontario Economy**

2.15 As part of their June 2021 Provincial Economic Forecast, TD Economics noted that the Province of Ontario was the one of the only provinces whose 2021 growth forecast was downgraded from the prior forecast. This was a result of the third wave in April and May, which was considered extremely harsh resulting in severe restrictions. The second factor, was production distortions in the auto sector owing to semi-conductor shortages were worse than assumed. This last factor is true for many industries as the global supply chain was disrupted by both COVID-19 and the Suez Canal blockage earlier this year.

2.16 TD still anticipates a strong rebound in the Ontario economy. Part of this anticipated growth is a result of the Province's "go-slow" approach to re-opening pushing activity into the second half of the year. The anticipated entrance into Stage 3, which loosened restrictions on retail and restaurants, was expected to grow the economy.

2.17 It is anticipated that the current spending by the Province will offer near term support, although it is expected that this will slow starting in 2022. Public capital investment is anticipated to increase both this year and next year. For the Municipality of Clarington, this may mean additional grants for capital investment.

2.18 TD Economics predicts a 5.4 per cent increase, year over year, in Real GDP in 2021 and 5.0 per cent in 2022. The unemployment rate is anticipated to go from 9.6 per cent in 2020 to 7.8 per cent in 2021 and down to 5.9 per cent in 2022.

2.19 Housing starts and pace of home renovations are expected to reduce from their 2020 and 2021 unusually high levels. This will have impact on future growth levels for the Municipality. While building permit revenues and development charges have been higher in 2020 and 2021, it is not likely sustainable at this level.

### Region of Durham Economy

2.20 Locally, the Oshawa CMA (which includes Oshawa, Whitby and Clarington) is expected to continue to see growth in real GDP of about 3.9 per cent in 2022 compared to 2021. Unemployment in the area is expected to decrease from 9.4 per cent in 2020 to 7.2 per cent in 2021 and 5.9 per cent in 2022. After 2022 it is anticipated to remain stable around 5.6 percent from 2023 to 2025.

2.21 The local CPI is anticipated, according to the Conference Board of Canada, to increase 2.45 per cent in 2022 compared to 2021. In 2023, the inflation is expected to be 2.1 per cent. The 2021 CPI is anticipated to end the year at 2.1 per cent, similar to the Bank of Canada’s forecast, over 2020.

## 3. Budget Calendar

### Overview

3.1 The budget sets spending guidelines and priorities for the Municipality's operating year of January 1 to December 31. It is beneficial to pass the budget early in the year to allow staff sufficient time to complete the capital plan and adjusting operating priorities.

3.2 Historically, the Municipality has passed its budget between late January and mid March. In September 2019, Council amended the Budget Policy to include that the budget ratification shall be targeted for the second Council meeting of any given year.

3.3 The 2021 budget process saw the need to have additional time for both the Special GGC deliberation day as well as the Council ratification. In setting the 2022 dates, Staff from Financial Services and Legislative Services discussed having “spill-over” days already established to ensure that calendars for both Members of Council and Staff could be set. The general public also benefits from knowing when the ultimate decision on the budget will be made. The 2022 dates were included in the revised Council meeting schedule which was approved on July 5, 2021.

**2022 Key Dates**

3.4 Based on the above, the 2021 budget calendar is as follows:

| Date | Event/Meeting |
|---|---|
| **October 15, 2021** | 2021 budget submissions from departments |
| **October 29, 2021** | 2023 to 2026 forecasts due from departments |
| **November 15, 2021 to November 26, 2021** | Department Head meetings with Treasurer and CAO |
| **January 14, 2022** | Release of draft budget book |
| **January 28, 2022 9:30am** | Special GGC Meeting – budget overview presentation and external agency presentations |
| **January 31, 2022 9:30am** | Special GGC meeting – Budget deliberations |
| **February 4, 2022 9:30am** | Special GGC meeting (if necessary) |
| **February 14, 2022 9:30am** | Council meeting – budget ratification |
| **February 18, 2022 9:30am** | Special Council meeting (if necessary) |

# Target Municipal Levy Increase

### Range Per Budget Policy

3.5 The Budget Policy outlined a range for tax levy increases based on a combination of the Consumer Price Index (CPI) and asset management requirements.

3.6 The low end of the range is set at 75 per cent of the CPI value plus 1.5 per cent as indicated in the asset management plan.

3.7 The high end of the range is set at 125 per cent of the CPI value plus 2.0 per cent as indicated in the asset management plan.

3.8 The July 2021 all items CPI was 3.50 per cent for Ontario. The following table outlines the Municipal Tax Levy increase range:

| Component | Low Range | High Range |
|---|---|---|
| **Consumer Price Index** | 2.63% | 4.38% |
| **Asset Management** | 1.50% | 2.00% |
| **Total** | 4.13% | 6.38% |

3.9 The July CPI reflects the increase in costs from July 2020 to July 2021, which included a recovery period from the first shut down. The recovery from the first shut down started in late June/early July and followed the significant drop in economic activity from March to June 2020. Therefore, whereas the 2020 July CPI was depressed because of the COVID-19 pandemic, this twelve month period is higher as a result of the recovery.

### Alternative Calculations

3.10 The COVID-19 pandemic had the result of a significant decrease economic activity from March to July (and even longer) of 2020. This resulted in 2020 there being a year over year change of 0 per cent, mainly a result of negative inflation in March to July 2020. As the economy recovered, the growth was higher than it normally would be as a result of the depressed months immediately after the start of the pandemic. This results in inflation numbers for 2021 which are likely higher than they otherwise would be as they included the recovery but not he negative numbers at the start of the pandemic.

3.11 In 2020 (for 2021), Staff recommended not using the calculation approved in the policy because the CPI was impacted significantly by the pandemic and was not reflective, in this case too low, of the inflationary factors that would impact the Municipality going forward. In 2021 (for 2022), Staff are again recommending not using the calculation approved in the policy because the CPI figures are impacted by COVID-19; however this time, it is felt that the inflationary indicators are too high for the cost likely to impact the Municipality in the following year.

3.12 Based on the economic forecasts for 2022 and the indisputable impact that the COVID-19 pandemic had on the first seven months of 2020, the CPI on July 31, 2021, is not a reasonable indicator of the cost of living impact for the 2022 budget. CPI is not a true reflection of the costs of the Municipality as it is impacted by consumer goods, food and other items that are not typically purchased by municipalities.

3.13 The annual non-residential building construction price index for the Toronto area (which does not include the Municipality of Clarington in its catchment) had a June 30, 2020 to June 30, 2021 change of 7.7 per cent. The Ottawa-Gatineau figure was 10.1 per cent. The use of a building construction index could be considered a more reasonable indicator of inflationary pressures for the Municipality than the consumer price index. Similarly to the CPI, the year-over-year will be impacted by the recovery of COVID-19 from the first wave.

3.14 Some municipalities utilize a Municipal Price Index (MPI) as their inflationary index. An MPI is determined by each municipality, there isn't a Statistics Canada index, based on their specific mix of goods and services purchased by the municipality. A drawback to this method is that it is not publicly available and requires staff to calculate the index manually. The City of Toronto has created a MPI calculation framework, for the years 2016 and 2017 the MPI was higher than CPI by 0.7 to 1.0 per cent.

**Recommended Target**

3.15 Staff recommend, again for 2022, that the impacts of the pandemic necessitate a departure from the approved budget policy as there has been an extraordinary event that has depressed CPI in 2020 resulting in an inflated result in 2021.

3.16 Staff are recommending that the inflationary factor for the determination of the budget target be based on the Bank of Canada’s forecast for CPI for 2022 of 2.2 per cent. Staff continue to recommend that the asset management factor of 1.5 per cent to 2.00 per cent be maintained to ensure that necessary capital investments can be undertaken in future years, capital investment is also a strong economic stimulus that will help the local economy in the post pandemic recovery.

3.17 The target be the mid-point of the range, this would indicate a target of 3.95 per cent which would include 1.75 per cent specifically to capital related costs.

3.18 Based on the 2021 municipal levy of $65,368,552, the target would provide approximately $1.4 for operating expenses (including transfers to reserves and reserve funds, and debt servicing payments) and $1.1 million for capital expenses; this would be in addition to new growth in assessment (NOT market growth which does not have an effect on the tax levy).

3.19 The Budget Policy also outlines that external agencies are limited to an increase of 150 per cent of the CPI. Therefore, for the 2022 taxation year, external agencies are capped at a maximum 5.25 per cent increase per the policy. Staff would recommend that 3.30 per cent be used for external agencies.

## 4. Key Assumptions for 2022

### Levels of Service

4.1 Staff are not, unless otherwise directed by Council, anticipating changes in the level of service to taxpayers and stakeholders of the Municipality of Clarington. There are no new services anticipated and no planned service eliminations. Certain services may be reduced due to demand related to COVID-19 but these are user fee supported programs.

4.2 While there are no anticipated changes in levels of service, there will be a report in the fall of 2021 regarding the long-term vision and roadmap for financial sustainability of hall boards, as previously directed by Council. There may be some additional costs associated with this roadmap; however, it is not anticipated that there will be changes to the level of services provided by these hall boards and arena boards.

### COVID-19 Impact

4.3 The current assumptions leading into 2022 will be that Community Services will see a slower first half of the year as a result of public health restrictions on facilities and rentals which should stabilize by the second half of 2022. Staff are not anticipating ever returning to the way in which we operated prior to COVID-19; however, it is anticipated that new levels of normal demand and operating costs will stabilize in the latter part of 2022.

4.4 Anticipated operating pressures include maintaining lifeguards while there could be reduced capacity for public swims, lower class sizes for aquatics and fitness programs to ensure social distancing. We anticipate that cleaning of our facilities will continue to be at standards not in place prior to COVID-19 and required personal protective equipment that may not have been standard prior to the pandemic.

4.5 The Planning and Development Services Department anticipates building and development levels to maintain at existing levels into 2022 thanks to the adoption of the secondary plans in 2020 and 2021 and the current housing demands in the Region.

4.6 It is not anticipated that COVID-19 will have an impact on other departments into 2022.

## 5. Concurrence

Not Applicable.

## 6. Conclusion

It is respectfully recommended that guidance on the target tax levy increase and any other changes to level of service be provided to allow Staff to prepare a draft 2022 Operating and Capital Budget which best meets the expectations of Council for deliberation.

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Staff Contact: Trevor Pinn, Director of Financial Services/Treasurer, 905-623-3379 ext. 2602, tpinn@clarington.net

Attachments:

Not Applicable

Interested Parties:

There are no interested parties to be notified of Council's decision.