2023 – 2025 Budgetary Pressures and Trends

ISSUE

As the City heads into its planning for the 2024 and 2025 Business Plan and Budget Cycle, there continues to be several budgetary pressures the City is facing. What are those pressures, how will they impact the 2024 and 2025 Business Plan and Budget and what are the options to address them?

BACKGROUND

History

As at the November 14, 2022 Governance and Priorities Committee meeting, when considering the 2022 Financial Forecast report, Committee resolved:

> "That the Administration report back in preparation for the 2024 budget with an evaluation of the risks and benefits of the discretionary hiring and spending freeze approach, as well as other budget pressures and trends."

As per the City's Multi-Year Business Plan and Budget Policy (Council Policy C03-036) the City Administration's first step includes estimating the expenditures and revenues in order to maintain the existing service level, including committed costs and Administrative portfolio priorities. This information is typically reported to Committee in the spring before the upcoming budget year.

CURRENT STATUS

Discretionary Hiring and Spending Freeze

The Covid pandemic financial impacts, higher than usual inflation, as well as savings targets included in recent budgets have put increasing pressure on the City's ability to achieve the expected service levels within the allocated resources. While the City's annual Service, Savings & Sustainability Report outline specific initiatives the City has undertaken to find efficiencies and savings, a discretionary hiring and spending freeze has also been a common tool used in the past several years to find additional savings. With 2022 consuming most of the City's stabilization reserves, Administration will rely more on hiring and spending freezes in 2023 to mitigate the absence of any financial backstops if a deficit were to be realized again.

The benefits of a discretionary spending and hiring freeze is that, together, they can result in significant short-term savings to the organization. Implications of ongoing spending and hiring freezes can include:

1. More expenditures in future years as many discretionary spending freeze items such as computer equipment, office furniture, inventory items and operational supplies are still required but their purchase is simply deferred to future budget years.
2. Employee morale and turnover issues as positions are held vacant and could result in unsustainable workloads and has the potential for increased overtime, for remaining employees.

3. With fewer resources available, work is reprioritized to focus on urgent and important items. Non-urgent and important items such as responses to non-critical auditor recommendations or internal control work may be deferred.
4. Unintended negative impacts to service levels may be realized as the administration holds positions vacant responsible for delivering these service levels.

Overall, the Administration tries to maximize potential savings while limiting the potential negative impacts. Therefore, a discretionary spending and hiring freeze has been used in recent years as opposed to an absolute freeze, which would produce more savings but also generate more negative impacts to the organization and service levels. While the Administration will push the boundaries of a hiring and spending freeze in 2023, achieving a sustainable budget is one of the Administration's highest priorities coming out of the Pandemic. Future budget discussions and recommendations will reflect this need.

<u>2023 Budget Pressures and Trends</u>

As previously communicated during budget deliberations, the 2023 budget made significant strides in becoming more sustainable through appropriate allocations for gasoline, diesel, energy and natural gas in addition to a reduction to the negative contingency or corporate savings target currently held within the budget. However, there remains significant budgetary pressures in 2023 that include:

1. $5.5 million savings target or negative contingency built into the 2023 budget;
2. Recovering operating revenues;
3. $2.6 million Information Technology Structural Budget Issues; and
4. Higher than normal inflationary pressures.

As explained, the Administration has already directed a stricter than normal discretionary hiring and spending freeze for 2023 to mitigate these pressures. The Administration will report back in mid-year regarding a 2023 financial forecast update.

DISCUSSION/ANALYSIS

<u>2024 Budget Pressures and Trends</u>

While the requirements of the City's Multi-Year Business Plan and Budget Policy are about to get underway by the Administration, there are several unique challenges facing the 2024/2025 Business Plan and Budget Cycle that warrant earlier reporting and potential direction. An overview of these specific pressures is outlined below.

<u>Post-Pandemic Revenue Recovery</u>

One of the most significant impacts to the 2024 and 2025 Budget is the slower than originally estimated return of operating revenues. When the Pandemic began, there was a significant impact to City fee or charge-based operating revenues, such as Transit, Leisure Centres, Parking and Fines and Penalties. To maintain the existing service levels and avoid a significant increase to the property tax, one-time funding from a variety of sources was used in 2021, 2022 and 2023 to offset the revenue impact. It was anticipated that by 2024, operating revenues would return to pre-pandemic levels and one-time funding would no longer be required. The one-time funding sources and amounts that were included in the 2021 – 2023 budgets are as follows:

- 2021 - $19.1 million from the Federal Safe Restart Program;
- 2022 - $13.9 million from the reallocated Investing in Canada Program (ICIP); and
- 2023 - $10.0 million from the reallocated Investing in Canada Program (ICIP).

To achieve the original fiscal plan, the City would need to see a $10.0 million increase in operating revenues from 2023 to 2024 to offset the removal of the one-time funding. Although the City continues to see a positive trend in revenues returning, based on a preliminary review, a full return to pre-pandemic revenues in 2024 is unlikely. Detailed work and analysis are ongoing by Administration to determine the exact impact in 2024 and will be reported as part of the indicative rate presentation in spring 2023.

Funding Plan Phase Ins

The City has previously approved several funding plans to complete key civic projects. These funding plans typically include a combination of property tax funding, government funding, transfers, and debt. Currently, there are two funding plans that require property tax phase in's that have been previously approved in principle but deferred during the pandemic. These are the Bus Rapid Transit Funding Plan and Recreation Game Plan. Phase in requirements are listed below:

Funding Plan	**2024**	**2025**	**2026**
Bus Rapid Transit	$460,000	$460,000	$650,000
Recreation Game Plan	$250,000	$250,000	$250,000
Total	**$710,000**	**$710,000**	**$900,000**

To ensure the appropriate funding is in place to meet the capital expenditure needs, it is important these phase ins are completed. With capital projects coming closer to fruition, it becomes more difficult to continue to defer these phase ins.

Information Technology Base Budget Gaps

As reported during the 2023 Budget Deliberations, the Administration identified several Information Technology Structural Budget Issues that need to be addressed. The Administration was hopeful through negotiations and other strategies these would be mitigated over time; however, it has become evident these are an ongoing annual requirement for the City of Saskatoon. Approximately $2.6 million of ongoing structural budget shortfalls related to Microsoft Licenses, Cyber Security and Project Management were identified during the 2023 Budget Deliberations reporting. These pressures will need to be addressed in future budgets.

Targeted Savings / Negative Contingency

In addition to the challenges identified in this report, through previous budgets the Administration has been tasked with finding savings targets to mitigate property tax impacts. While the Administration is committed to finding savings and efficiencies as evidenced by the annual reporting on Service, Savings and Sustainability (SSS) these savings have largely been one-time savings through deferral of projects, training and hiring or efficiency savings that build capacity as opposed to reduce budgets.

Included in the 2023 budget is approximately $5.5 million in negative contingency or targeted savings. While the Administration has evidenced savings results in the past, the savings target combined with the other pressures has placed additional pressure on the budget to achieve expected results.

Fusion Program

The Fusion implementation is currently being funded through a capital project, and funding is expected to be fully depleted by the end of 2023. The program has some base operating funding built up through savings and phase ins, however, it is not sufficient to complete the work remaining to fully implement the system.

While the implementation of Fusion came with the goal of achieving significant savings, efficiencies, and improvements in controls, there is still much work to be done to fully realize these improvements. Continuing to support the Fusion work is critical to the ongoing improvements of the system and City processes overall. A funding source for the continued implementation and stabilization of the Fusion system will be required in 2024.

Unknown Multi-Material Stewardship Western (MMSW) Funding Impacts

Discussions regarding the future of the MMSW funding are currently ongoing between the Administration and the Province as part of the introduction of The Household Packaging and Paper Stewardship Program Regulations. The most extreme impact would be that the Province takes over recycling services for the Province and funding would not be provided to Municipalities. This is a potential issue based on the way the City uses the MMSW funding within our budgets. The following allocation are examples that could have mill-rate implications if the funding is withdrawn:

- $485,000 being utilized to repay debt on Recovery Park;
- $1,100,000 being utilized to subsidize the compost depots; and
- $160,000 being utilized to subsidize the Household Hazardous Waste Days.

If MMSW funding were removed or restrictions put in place to direct how the funds must be used, in order to continue providing the above services, operating funding would need to be allocated.

Recovery Park

Recovery Park has been previously identified as having an operating impact, once the capital construction is complete, to appropriately operate the facility. With construction scheduled to be completed in 2023, the capital project is expected to carry the operating impact for this year, however, a plan or phase-in is required to fund the operations in 2024 and beyond.

Saskatoon Fire Department Phase-in
As identified in the Saskatoon Fire Master Plan, there is a need for two new Fire Halls to maintain existing service levels. While the capital funding has not yet been finalized, the projects are being included in the 2024-2035 Major Capital Prioritization Process and likely to receive some level of funding over the next five years. As such, and in line with previous direction provided by City Council, step growth should be phased in starting in the 2024 budget year to avoid a significant funding requirement in the year they become operational.

Snow Removal Phase-In
Up to $20.0 million in borrowing was approved as part of the January 25, 2023 regular meeting of City Council to fund the 2022 Snow and Ice Emergency Response (2022 Roadways Emergency Response Funding Plan Options). While the exact details of the repayment plan are the subject of a future report, it was directed to the Administration that a portion of this repayment as well as the development of a fund for future events will be mill-rate funded. The report outlined up to $2.1 million in annual phase-ins would be required and will be part of 2024/2025 Budget Deliberations.

Higher than Typical Inflationary Pressures
In addition to the base issues identified as we head into 2024, the City will be faced with higher inflationary pressures than in past budgets. While significant strides were made as part of the 2023 budget to address fuel and energy cost increases the inflationary impact to other contracted services were not adjusted. The Administration is currently going through a detailed analysis of 2024/2025 budget requirements to maintain existing services which will form a part of future budget reports and may require higher than normal inflationary adjustments.

Municipal Revenue Sharing
On a positive note, the City does expect to continue seeing significant annual increases in the Municipal Revenue Sharing (MRS) grant based on the current formula and current Province of Saskatchewan economic forecasts. Based on existing forecasts of provincial sales tax revenues, we estimate annual increases to the MRS of $5.1 million in 2024 and $4.0 million in 2025, which will help to offset some of these financial pressures. It should be noted that these estimates and projections are revised periodically based on the economic conditions in Saskatchewan.

FINANCIAL IMPLICATIONS
Financial implications are included within the body of this report. Additional budget information will be brought forward as part of the Indicative Budget process in spring of 2023.

NEXT STEPS
While the Administration continues to work through the detailed analysis and requirements for the 2024 and 2025 budget, it is evident many of the financial impacts of the pandemic, base budget issues, funding plan requirements, higher than normal inflation and savings target pressures will be coming to a head during the 2024/2025

budget preparation and presentation. The Administration's current plan is to go through the refinement of the budget and push the boundaries on resource requests to deliver services in 2024/2025 keeping in mind the current financial realities and the need to ensure the budget is sustainable and achievable.

The Administration welcomes any additional information or direction from Committee regarding the remainder of the 2024/2025 budget process. If Committee wishes for additional reporting, options, or a different governance process than what is outlined in the Multi-Year Business Plan and Budget Policy, there is currently ample time before budget deliberations to change course or enter a more detailed review earlier in the process.

REPORT APPROVAL

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