

Request for Decision

Capital Budget - Inflation Options

Presented To:	Finance Committee
Presented:	Tuesday, Nov 08, 2011
Report Date	Thursday, Nov 03, 2011
Type:	Managers' Reports

Recommendation

THAT the Finance Committee direct staff to prepare a budget option in accordance with Option 2 which would amend the existing capital policy and increase capital envelopes by the Non-Residential Building Construction Price Index (NRBCPI) effective for the 2012 Budget in accordance with report from CFO/Treasurer dated November 3, 2011.

Financial Implications

Option 1 – Status Quo: No further budget increase since the 2% inflation factor has been applied to the Capital Envelopes in the 2012 Budget.

Option 2 – Increase by NRBCPI: If the budget option is approved, the 2012 budget would increase by an additional \$1.3 million combined on the tax levy and W/WW user fees. In addition, future budgets will increase by a similar amount.

Purpose of Report

The purpose of this report is to respond to Council's resolution from the October 5, 2011 Finance Committee meeting, as follows:

“that to maintain the status quo, Council's policy that stated “contributions to capital envelopes would increase by an inflation factor annually of 2%” be proposed to read “contributions to capital envelopes would increase according to the Non-Residential Building Construction Price Index” and further that staff bring back a report to alter the existing policy and a budget option for the November meeting. Staff would need to do an analysis that Non-Residential Building Construction Price Index is the best index to use in this instance”.

Historical Capital Funding

There are continued capital funding pressures due to the age and condition of the City's infrastructure assets that require replacements and/or improvements in addition to residential, commercial and industrial growth demands.

Signed By

Report Prepared By

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Digitally Signed Nov 3, 11

Recommended by the Department

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Recommended by the C.A.O.

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A Long Term Financial Plan (LTFP) was adopted in principle by Council in November of 2002. One of the assumptions in this Plan was that the contributions to the Capital Envelopes would increase by an inflation factor of 2% annually. A 2% inflation factor was first applied to the 2004 envelopes, and has been maintained since then.

One of the general supporting policies in order to “Ensure Long Term Financial Sustainability” from the LTFP relating to capital investments is to “raise sufficient revenue to meet long-term ... capital requirements, recognizing that inflation increases the cost of capital programs. **Recognition of inflationary pressures will ensure services and programs are not eroded by shrinking real dollars.**”

Comparison of Cost Indexes

There are many different inflation measures and indices; however the two listed below provide the best inflationary estimates for capital investment projects.

An overview and impact is provided below for the Consumer Price Index and the Non-Residential Building Construction Price Index options as an inflationary index.

Consumer Price Index (CPI)

- a. The Consumer Price Index (CPI) is an indicator of the changes in consumer prices. The CPI measures price change by comparing, through time, the cost of a fixed basket of commodities. Since the basket contains commodities of unchanging or equivalent quantity and quality, the index reflects only pure price movements.
- b. This index includes all the following major components: food; shelter; household operations, furnishings and equipment, clothing and footwear; transportation; health and personal care; recreation, education and reading; alcoholic beverages and tobacco products.
- c. This index is publicly available on Statistics Canada website and is updated on a monthly basis.
- d. This index is not recommended as it does not include any directly related factors for capital construction projects. The impact of increasing the inflation factor from 2% to 3.2% would result in an additional increase to the budget of \$680,000 for 2012 on the tax levy and W/WW user fees.

2. Non-Residential Building Construction Price Index (NRBCPI)

- a. This index is a quarterly series measuring the changes in contractors' selling prices of non-residential building construction (ie. commercial, industrial and institutional). The indexes relate to both general and trade contractors' work and exclude the cost of land, land assembly, design, development and real estate fees.
- b. This index helps in the interpretation of current economic conditions and is of particular interest to governments undertaking economic analyses and users concerned about the impact of price changes on capital expenditures. Other uses include, updating construction project costs through escalation and forecasting financial requirements for proposed projects.
- c. This index is publicly available on Statistics Canada website and is updated on a quarterly basis.

- d. The City's Development Charges rate is adjusted annually using this index as it best reflects changes in construction costs.
- e. This index is recommended as it best reflects changes in capital construction costs. Also, this index will maintain the current level of capital infrastructure deficit as annual increases to capital funding will keep pace with expected increases in capital construction costs. For 2012, the budget impact would result in an increase of approximately \$1.3 million, 0.4% increase to the levy and 1.1% increase to WWW user fees.

Please refer to Appendix A that provides the summary of these cost indexes back to 2005 along with comparison to historical inflations to the annual capital envelopes.

Options for Finance Committee

Option 1: Status Quo

Maintain existing capital policy which increases the Capital Envelopes by 2% to approximate inflation. This has been incorporated in the 2012 Base Budget.

Option 2: Non Residential Building Construction Price Index

Amend the Capital Policy and increase the capital envelopes on an annual basis in accordance with the greater of 2% inflation or the Non-Residential Building Construction Price Index (NRBCPI). As outlined in Appendix B, using the NRBCPI for the 2012 Budget would increase the capital envelopes by an additional 2.4% to 4.4%. For the 2012 budget, this would require a capital enhancement of approximately \$1.3 million; \$796,000 or 0.4% increase to the municipal tax levy; and \$538,000 or 1.1% increase to WWW user fees.

Summary

Staff recommends Option 2 which is the use of Non-Residential Building Construction Price Index (NRBCPI) to increase Capital Envelopes on an annual basis effective with the 2012 Budget. This cost index directly relates to cost of capital construction projects and will assist the City in maintaining the current level of infrastructure deficit. In addition, recognition of these inflationary pressures will ensure capital investments are not eroded by shrinking real dollars.

The majority of the increase relates to Roads and Water/Wastewater in the amount of \$1.1 million with the remaining balance to other departments.

Appendix A - Summary of Cost Indexes

	Consumer Price Index - Inflation (Canada)	Non-Residential Building Construction Price Index (Ottawa)	Council Approved Increase to Capital Envelopes
Published by	Statistics Canada	Statistics Canada	
Most Recent Rate Available (Month)	September 2011	Second Quarter 2011	
Most Recent Rate Available	3.2%	4.4%	2.0%
Historical Rates as of:			
Most Recent Rate for 2011	3.2%	4.4%	2.0%
December 2010	2.4%	2.0%	2.0%
December 2009	1.3%	-1.6%	2.0%
December 2008	1.2%	8.7%	2.0%
December 2007	2.4%	5.6%	2.0%
December 2006	1.7%	6.4%	2.0%
December 2005	2.1%	4.3%	2.0%
7 Year Average	2.0%	4.3%	2.0%

Appendix B - Increase to Capital Envelopes from 2% Inflation to NRBCPI of 4.4%

Department	Option 1 - 2012 Capital Envelopes Including W/WW and Police (2% Inflation)	Option 2 - 2012 Capital Envelopes with NRBCPI of 4.4%	Increase from 2% Inflation to NRBCPI rate of 4.4%
Infrastructure			
Roads	\$ 24,497,611	\$ 25,074,026	\$ 576,415
Water / Wastewater	\$ 22,845,973	\$ 23,383,526	\$ 537,553
Transit	\$ 526,674	\$ 539,066	\$ 12,392
	\$ 47,870,258	\$ 48,996,618	\$ 1,126,360
Community Development		\$ -	\$ -
Leisure and Citizen Services	\$ 3,413,530	\$ 3,486,189	\$ 72,659
Health & Social Services	\$ 714,000	\$ 730,800	\$ 16,800
	\$ 4,127,530	\$ 4,216,989	\$ 89,459
Growth and Development		\$ -	\$ -
Environmental Services	\$ 867,000	\$ 887,400	\$ 20,400
Facilities	\$ 1,428,000	\$ 1,461,600	\$ 33,600
Planning	\$ 112,200	\$ 114,840	\$ 2,640
Growth Related Projects	\$ 200,000	\$ 200,000	\$ -
	\$ 2,607,200	\$ 2,663,840	\$ 56,640
Emergency Services		\$ -	\$ -
Fire	\$ 1,020,000	\$ 1,044,000	\$ 24,000
Emergency Management	\$ 10,200	\$ 10,440	\$ 240
CLELC	\$ 10,200	\$ 10,440	\$ 240
	\$ 1,040,400	\$ 1,064,880	\$ 24,480
Administrative Services		\$ -	\$ -
Information Technology	\$ 204,000	\$ 208,800	\$ 4,800
Administration	\$ 127,500	\$ 130,500	\$ 3,000
ERP Peoplesoft Projects	\$ 333,240	\$ 333,240	\$ -
Furniture	\$ 102,000	\$ 104,400	\$ 2,400
	\$ 766,740	\$ 776,940	\$ 10,200
		\$ -	\$ -
Healthy Communities Initiatives	\$ 600,000	\$ 600,000	\$ -
		\$ -	\$ -
Police Services		\$ -	\$ -
Police	\$ 534,169	\$ 546,738	\$ 12,569
Communications Infrastructure	\$ 891,900	\$ 906,180	\$ 14,280
	\$ 1,426,069	\$ 1,452,918	\$ 26,849
		\$ -	\$ -
TOTAL	\$ 58,438,197	\$ 59,772,184	\$ 1,333,987
Increase in Tax Levy Capital Envelopes			\$ 796,434
Increase in W/WW Capital Envelopes			\$ 537,553