HALIFAX
REGIONAL MUNICIPALITY

Working Draft

REGIONAL MUNICIPAL PLANNING STRATEGY

for Public Consultation

Halifax Regional Municipality
Regional Planning
PO Box 1749
Halifax, N.S. B3J 3A5
Tel: 902 490 5857
Fax: 902 490 5730
E-mail: regplan@halifax.ca
www.halifax.ca/regionalplanning

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CHAPTER 11: FINANCE

11.0 INTRODUCTION

Municipal Governments exist to provide services to its citizens. In doing so, it is critical that HRM has sound financial management practices and adequate financial strategies to deal with the issues the municipality faces. The Multi-Year Financial Strategy which Council approved in 1998 has served the municipality well as have other key initiatives such as Tax Structure Reform, the existing Revenue Strategy and the Three-Year Capital Planning process. Under these initiatives, HRM has seen a sharp decline in its debt, an upward trend in reserve balances and Capital from Operating ("Pay as you go") funds and expenditure levels constrained to match the growth in the region as well as inflation. Planning and budgeting have become increasingly sophisticated, being currently led by HRM's Corporate Scorecard.

Despite this, HRM faces a series of financial risks and opportunities. The Regional MPS offers a chance to re-orient financial and taxation strategies to ensure that they are first of all, consistent with the rapid growth HRM has and will continue to experience and second, that they are placed within a long-term context which is growth sensitive. At a minimum, HRM's revenue strategy for the future must encourage sustainable growth, allocate costs appropriately, create a truly competitive taxation environment and respect individual differences in ability to pay.

Residents who live in existing or older communities in HRM and those who live in new communities have every reason to assume that their municipal infrastructure needs, appropriate to their community, will be provided over a reasonable period of time. They should also be able to assume that this infrastructure, once built, will be maintained. This is only an achievable assumption in the long-term, if we plan our growth in both existing and new communities in such a way which we create the communities we want for the future. To do otherwise ensures that existing infrastructure will deteriorate, new infrastructure will lag well behind demand and costs to support both will be higher and less affordable.

A review of the existing environment shows that six critical areas pose HRM with both a very clear risk to the future, but also a potential opportunity to improve its long-term financial position.

These six critical risk areas are:

1. The Risk of Unplanned Growth

Individual cost drivers, policy or regulatory limitations, local geography and settlement patterns can all affect cost differently. Costs are driven not just by density but also by distance from key service points, dispersion patterns and the diversity in land uses. Collectively, these are referred to as the "Four Ds".

Analysis undertaken for the Regional MPS clearly shows that the marginal costs of some of HRM's current settlement patterns are greater than the average costs. Growth patterns which reflect large lot sizes and frontage have a significant impact on the cost of the delivery of municipal services. Distance travelled and the length of the infrastructure connecting individual dwelling units result in high costs per dwelling unit. This trend implies a disturbing future of greater cost pressures and an increasing inability to provide services to the public. The objective here is not necessarily to provide municipal services at the least cost, but to provide the required services at a reasonable and sustainable cost, that citizens are willing to pay for through municipal taxes and other charges.

2. The Infrastructure Capacity Gap

Like many municipalities, HRM has a sizeable Infrastructure or "Capacity Gap". The Capacity Gap is the difference between the amount of debt and operating funds required to maintain HRM's Assets and the debt and operating funds it has available under its current financial strategies. Currently, HRM estimates its Capacity Gap to be approximately $30 million on an annual basis. Narrowing the Capacity Gap is strongly linked to the Regional MPS. First, existing assets - roads, sewers, public transportation etc. - represent a significant portion of the Capacity Gap. The more pervasive the existing infrastructure gap, the higher the maintenance costs and the lower the public satisfaction. Secondly, the rapid growth that HRM has and continues to experience has placed a strong demand on HRM for new capability assets. New subdivisions require infrastructure and services ranging from water and sewer to playgrounds. Thirdly, those very same new assets will eventually require replacements. The new street in a new subdivision will itself need to be re-surfaced and replaced. Proper planning and settlement form not only decreases the demand for new assets; more importantly, it reduces the need to operate, maintain and eventually replace those assets.

3. Fair and Equitable Relationships

Available data suggests HRM is more dependent upon property tax as a source of revenue than any other major city in Canada. In many Canadian provinces, substantial funding is available to municipal governments either through unconditional and other grants or through transfers of tax revenues such as fuel taxes. The Province of Nova Scotia provides a number of municipal programs (such as for equalization purposes). However, the difficult financial situation of the Province of Nova Scotia has precluded any significant benefits being available to HRM. It is estimated that HRM receives only 1.4% of its funding from other levels of government, lower than most, if not all, major cities in Canada. In fact, Nova Scotian municipalities fund a significant portion of the costs of provincial responsibilities, such as education, corrections and the assessment system through property taxes, even though income taxes may be the more appropriate revenue tool.

Also critical in examining this issue is HRM's relationship with other municipalities in Nova Scotia, including Cape Breton Regional Municipality, and the 53 other municipal units. The needs of residents across the Province differ from community to community; however, the need for predictable, appropriate funding levels from senior levels of government does not.

Recent actions at the Federal level open many new opportunities for HRM. The Federal sharing of fuel tax and the expected extension of infrastructure programs should help HRM deal with some of its critical financial shortages. Such actions offer significant opportunities which HRM can build upon. As we address the impact that funding from other levels of government has on municipal services, taxpayers will expect that municipal, provincial and federal governments work together to serve their needs. All levels of government must share in the costs of delivering against common goals.

4. HRM Competitiveness

The long-term economic prospects of any municipality depends on the health, vitality and competitiveness of its commercial sector. This has particular significance in HRM, the capital of the Province. Municipalities must pay attention to their competitiveness or risk losing both existing and potential businesses. Municipal government impacts upon the competitiveness in a number of ways but most directly through the services it provides and through the taxation it levies to pay for those services.

The combined commercial/business occupancy tax rate in HRM may be as much as four times as high as the comparable residential tax rate. Services to commercial enterprises are generally comparable to those that residents receive although they are often not the same type or level of service. All of this raises important questions as to the long-term competitiveness of the way HRM taxes and provides services and whether the structures that exist are sensitive to growth. Elimination of the Business Occupancy Tax is an important step on the road to a more competitive business environment.

5. Residential Taxation

Residential taxation is one of the most controversial and critical areas a municipality has to deal with. At the heart of residential taxation is the “market value” appraisal system. Under this system, households pay property tax based upon the market value of their property. Market value is widely recognized as the most technically correct basis for property taxation and there is every reason to believe that Nova Scotia’s market value system provides reasonable estimates of property values. The issue for municipalities, however, is whether market value is the proper or only basis for taxation to encourage sustainable growth, allocate costs appropriately, create a truly competitive taxation environment and respect individual ability to pay.

The difficulties of market value taxation are not solely limited to HRM or to Nova Scotia. As it grows, however, the challenges have become more severe within HRM. The uneven distribution of market growth has made it increasingly difficult to establish budgets and tax rates that are understandable and fair to residents. Nearly 8% of HRM dwellings are located on waterfront properties which have experienced significant market value increases in recent years. On the Halifax peninsula, the proximity to downtown combined with its natural boundaries, has caused values to rise sharply irrespective of municipal services, costs or ability to pay. While these properties experience market increases, other neighbourhoods see only moderate increases or declines. It is this smattering of market increases far beyond the average and with no direct relationship to municipal services, which makes setting a tax rate which fairly distributes costs to residents impossible.

As noted, the other aspect of property taxation is the levying of the rate. HRM has the authority to levy an urban, suburban and rural tax rate and to levy area rates. This provides HRM with geographic flexibility. However, efficient forms of land use cannot be taxed at preferential rates nor can development of brownfield or greenfield sites. High-density developments must be taxed at the same rate as their neighbours even though the cost of providing identical services may be much lower. As such, the tax system appears to penalize efficient low-cost forms of development and discourage opportunities for smart growth while inadvertently encouraging inefficient development patterns. The result has been a trend toward forms of development that do not take into account the relative costs of service delivery. Residents then face delays in the provision of adequate services and affordability issues.

The present HRM tax structure makes it difficult to achieve an efficient distribution of services. Communities wishing to acquire better transportation or infrastructure are often required to pay a significant portion of the investment and operating costs directly, even though the benefits of such services may be widespread across the municipality. As a disproportionate share of tax revenues are levied on commercial establishments, such investments often tend to occur when a high commercial tax base co-exists with such needs. For the Regional MPS to become truly effective, a means must be found to share the costs of municipal services across all of those who truly benefit without unduly encouraging inefficient growth patterns.

In addition to property tax, a wide variety of other forms of tax are available to HRM. These include various charges and fees, local improvement charges and infrastructure fees. The most significant of these are the Deed Transfer Tax and the Capital Cost Contribution (CCC). HRM's revenue base and tax structure must, at a minimum, not work contrary to the Regional MPS. Over time our taxation and financial policies must encourage sustainable growth so as to create a consistent foundation which supports the Regional MPS outcomes.

6. Community Expectations

Lastly, community expectations form a major factor for any long-term financial plan to succeed. If citizens cannot be provided with enough long-term information such that they can reasonably understand what services and costs they will face under specific housing choices, then a strong sense of entitlement will prevail even though this may be at odds with the stated intentions of the Regional MPS.

F-1 HRM shall create a Finance Functional Plan to address issues concerning:
- a) Revenue Strategy:
  - (i) Property taxation (residential & commercial)
  - (ii) Other forms of taxation & charges
  - (iii) Broad fiscal policies
- b) Financial Impacts and assumptions of this Plan.

11.1 HRM'S REVENUE STRATEGY

To support the Regional MPS and the need for a predictable appropriate revenue stream to support municipal services now and in the future, HRM has embarked on a review of its revenue and fiscal strategies. There are three main elements to this Revenue Strategy. The first relates to property taxation and broad forms of taxation; the second, to other, more specific forms of taxation and charges; and the third, to broad fiscal issues including the management of debt, reserves and capital. Collectively this strategy is designed to ensure that HRM's fiscal strategies and processes support and encourage the outcomes of Regional MPS.

11.1.1 Property Taxation (Residential and Commercial)

In no other level of government are taxation and service so linked as they are in municipal government. Taxes are viewed as being directly linked to services the municipality provides to residents. With the ever fluctuating assessment base, there is a legal requirement and an expectation that a property tax rate will be set each year. Interestingly, this is unlike expectations around income or sales taxes.

In this area, there are a number of critical imperatives which need to be accomplished. As approved in the 2005-2006 Budget, HRM is embarking on a review of property taxation. As part of the 2005/06 budget, Council approved the institution of a one-time tax credit for dwelling units with higher than average assessment growth. This is not a long-term reform measure but simply a means to take the pressure off those residents with higher than average assessment increases. For future years and the longer term, HRM must examine its reliance on the market based property tax. To the extent that HRM relies on property or other tax, it is critical to ensure that the system be sensitive to the growth policies within the Regional MPS.

F-2 Through the Functional Plan, HRM shall:

1. Research, analyze and recommend tax reforms (including possible legislative changes) which reflect an appropriate balance between market based property taxation and other charges, and that: (1) is rational and transparent respecting services available to the community, now and in the future, and taxes paid (2) ensures a competitive local government taxation environment (3) considers the relationship between tax burden and the ability to pay;
2. Ensure that any tax system reforms include appropriate levels of taxation to encourage efficient forms of development and consider incentives for brownfield development and does not encourage the additional development of inefficient patterns of development;
3. Ensure the tax system provides stable, appropriate revenue streams to allow for the long-term growth of the municipality. These should recognize and encourage the demographic and economic growth within HRM;
4. Research the commercial tax burden including (1) appropriate benchmarks to other jurisdictions, (2) its relationship to the cost and mix of services provided, and (3) the

impact of which burden on economic growth and development and provide Council with any appropriate recommendations; and

5. Research the Deed Transfer Tax and its relationship to economic growth and provide Council with any appropriate recommendations.

11.1.2 Other Forms of Taxation and Charges

While property taxation is currently the most powerful tool available to HRM, other taxes and charges have extremely significant impacts upon the delivery of critical infrastructure and hence, the development of efficient settlement patterns. The provision of water service is a regulated service performed at arms length through a utility; however, sewer service remains an unregulated service very closely linked to the provision of water. The funding of HRM's sewer services is dependent upon a variety of taxes and fees. In order to support Regional MPS outcomes, these charges and fees must be examined to ensure they encourage long-term sustainable growth in the municipality. Such fees and charges under HRM by-laws such as the Trunk Sewer Charge, Sewer Development Charge, Local Improvement Charges, Pollution Control Charge and the Capital Cost Contribution (CCC) all contribute to the development and operation of the sewer system. (CCC must also be examined to determine the balance of services included in the charges, for example, with transit). These charges all interact to allow for the funding of the various sewer components.

Through the Finance Functional Plan, HRM shall:

1. Investigate and identify ways to integrate the funding of water and sewer services so as to ensure the most efficient development and use of that infrastructure;
2. Review and update the various sewer taxes, fees and charges under HRM by-laws to ensure they encourage the development patterns and infrastructure investments being proposed under the Regional MPS; and
3. Research and assess the impact on housing affordability of charges levied on lot development and home sales and purchases.

11.1.3 Broad Fiscal Policies

If planned services drive taxation and revenue policies, then those revenue policies cannot be reviewed in isolation of the underlying fiscal issues and processes. HRM has specific policies and strategies which relate to fiscal management, debt, reserves and budgeting. These need to be reviewed to ensure they function in a growth environment and are consistent with the Regional MPS. In addition, HRM needs to aggressively seek out new sources of Federal, Provincial and other cost-shared funding.

Current debt policies restrict the issuance of debt to 80% of the principal being re-paid in a year. The underlying assumption is that as debt declines, financial capacity currently allocated to interest costs can be used to provide broad fiscal capacity. The current policy has seen continuous steady declines in debt. However, a long-term focus on debt and its relationship to growth has not been established. For instance, it may be in HRM's long-term interest to match the change in debt to the growth in the municipality; hence, allowing for the more rapid development of the infrastructure which services its growth. More broadly, there are no long-term targets for debt levels or provisions as to how to use that capacity.

Through the Finance Functional Plan, HRM shall:

1. Establish a 25 year debt plan with debt targets; and
2. Investigate the relationship of debt to growth to ensure both the most efficient allocation of resources and that stable patterns of growth are supported.

Reserve adequacy is of critical importance for HRM in managing infrastructure demands against fiscal health. It is clear that while reserve contributions have increased considerably in the past 8 years, they remain insufficient to either sustain HRM's infrastructure and operations or to allow for the infrastructure needs of growth. Due to lack of available capacity, some necessary reserves are either underfunded or have yet to be established.

Through the Finance Functional Plan, HRM shall:

1. Establish a reserve framework which provides a rational structure for the development of reserves and their sensitivity to various drivers such as growth or economic change;
2. Establish each reserve recommended under the Reserve Framework, even where funding is not immediately available. It should also provide regular estimates of the funding and balance targeted for each of its reserves and the resulting "Reserve Gap"; and
3. Investigate linking reserve allocations to changes in growth and other factors.

Capital Planning within HRM has progressed rapidly within the last three years. HRM now uses a three year capital plan and provides allowances for the eventual operating costs of new assets. In addition, HRM is developing long-term estimates of the funding required to maintain its existing assets and the investments required to provide services for the growth HRM is expected to see over the life of the plan.

It is imperative that HRM create a long-term capital plan so that it can begin to make provisions today for investments which will be required in the future. The Regional MPS provides a way forward that moves HRM away from an unsustainable future. For instance, in order to achieve the community, economic and financial benefits of the plan, infrastructure investments are required that place greater emphasis on public transportation. The creation of a full long-term capital plan will require considerable revisions to the current systems of budget and business planning. Before HRM can balance the long-term funding which will be available to the long-term demands, it needs to fully understand that environment. Part of this environment are changes requiring local governments to follow Public Sector Accounting Board (PSAB) standards as the basis for accounting rather than the existing Municipal Accounting and Reporting Manual for Nova Scotia municipalities. These rules will influence the accounting and management of HRM's resources.

Through the Finance Functional Plan, HRM shall:

1. Create a long-term 25 year Forecast of Demand which allows HRM to investigate and model various funding options and strategies for both capital and operating. This will include estimates of Capital demand, related operational requirements and estimated available funding, both operational and capital and will detail funding gaps that exist;
2. Complete the State of the Physical Assets project. This information is an important element of any long-term asset recapitalization plan;
3. Create a long-term 25 year Capital and Operational Plan which is based on the Forecast of Demand and Regional MPS growth scenarios with required funding plans. This will require substantial revision to budgeting and planning systems and may require an extensive planning period to complete;
4. Implement the required Public Sector Accounting Board standards; and
5. Ensure that HRM advances the economic and financial benefits of this Plan to others levels of governments and seeks to secure improved partnerships and funding arrangements.

11.2 THE FINANCIAL IMPACT AND IMPLEMENTATION OF THE REGIONAL MPS

The Regional MPS offers a tremendous opportunity to save on future municipal costs. It does this in two chief ways. First, by its very nature, a planned situation allows costs to be controlled better. The HRM will be able to anticipate what infrastructure is required and when. This allows it to respond to expected events in advance, rather than scramble to react. For instance, future recreation, fire and other facilities can be located where they serve expected major population nodes. Road and transit service can be constructed to serve anticipated development. Advance planning allows it to acquire strategic parcels of land while they are still available and permits construction projects to take place in an orderly cycle. Necessary reserve balances can be built up in advance and public expectations can be better managed. By encouraging the right density in proposed developments and reducing the dispersion of and distance between communities, the costs of scattering developments across the region can be reduced. But also, more things become possible: transit becomes more feasible, mixed-use developments bring private services closer to residents and open spaces become "connected", creating more walkable, complete communities. By focusing growth on key areas (District Centres, Local Centres and Rural Commuter Centres), services can be provided more quickly across HRM, including rural and suburban areas.

The cost to provide the Regional's growth related services over the next 25 years will total $1.7 billion, $250 million less than under the expected Base Case. This benefit will be shared amongst HRM, other government levels and private property owners. On an annual basis it means that the pressure for HRM to spend more money just to maintain the same level of service will be reduced. It also means that HRM will be able to provide more and different types of services, more affordably. For instance, some form of transit service is being planned for all centre types: Regional, District, Local and Rural Commuter Centres.

11.2.1 Water and Sewer Service

The Regional MPS proposes to develop new suburban growth centres in a more strategic way which provides a serviced urban/suburban area with 20 years of growth potential. The Regional MPS focuses suburban growth in existing communities and two new growth centres – Morris-Russell Lake and Bedford West rather than ten or more potential greenfield sites. As well, it is anticipated that the additional 12,500 households on piped water/sewer services (in the Plan) would save on average about $750/ year on maintenance and repair of their on-site systems. The costs of the water and sewer systems (including potential remediation) are expected to decline by over $70 million over the next 25 years with the benefits and costs shared between HRM, the Halifax Regional Water Commission and private property owners with septic and well systems.

11.2.2 Transportation Services

The Base Case scenario would propose to temporarily remedy traffic congestion through new road expansion projects estimated at nearly $200 million. The Regional MPS policy integrates land use and transportation planning to provide greater transportation options to HRM residents and visitors, improve the commuting experience and allow for road building and improvements. The proposed balance of transportation capital projects – roughly half on roads and half on transit – would total over $150 million. This will save $75 million in major capital costs over the life of the Regional MPS. In total, reconfiguring growth and changing the current mix of transportation spending will save nearly $165 million over the life of the Regional MPS. It will also provide better service. Rather than expanding costly road networks, new transit solutions can be applied to the needs of citizens.

11.2.3 Fire Protection

The predictability of the future settlement patterns will allow fire services to better plan the location of rural stations when they are (re)built, therefore improving response and reducing costs. Approximately $4 million in combined capital and operating costs can be saved through the Regional MPS.

11.2.4 Park Land & Wilderness Protection

The Regional MPS emphasizes protection of wilderness assets and increased recreation opportunities and connected open space. In the Regional MPS, an additional $4 million dollars (over the Base Case) may be required to allow for the development of new regional parks, wilderness corridors and urban/suburban trails. Since communities develop in a more compact manner, more land is left in its natural state.

11.2.5 The Transition to a Planned Environment

While cost pressures are reduced across all sectors, there are a number of timing issues which must be dealt with. For instance, water and sewer costs are expected to decline by over $70 million over the life of the plan. During the first ten years of the Plan, however, it is expected that there will be a considerable up-front investment into water and sewer infrastructure. HRM has a variety of tools available for this investment including the Capital Cost Contribution (CCC), Local Improvement Charges (LIC), the CCC and other sewer related fees. The planning for this investment and the exact tools involved is a major thrust of HRM's Revenue Strategy

In Years 10 to 15 of the Plan, substantial investments are required in the transit system in order to achieve the savings that will come from reduced road construction. While more debate and research is required before final recommendations can be made to Council, there are a number of options which might be explored in full or in combination to ensure that this investment occurs. These include:

1. re-priorizing the capital plan to include higher transit investment;
2. extending the Capital Cost Contribution (CCC) to transit infrastructure including the introduction of new transit lines as envisioned by the Regional MPS;
3. allocating federal fuel transfers to transit. (HRM is expected to receive $70 million over five years and has allocated only $24 million); and,
4. using future operating capacity freed up due to declining interest costs. This capacity is being created due to HRM's declining debt.

The challenges in making the transition from an uncontrolled and somewhat unplanned environment are significant but can be overcome. The Regional MPS provides a framework for the delivery of services which is financially sustainable and achievable. The Revenue Strategy now underway within HRM provides extra confidence that future growth can be properly managed and the goals and objectives of the Regional MPS can be accomplished.

Changing the trend in existing settlement patterns within HRM requires a lot of forethought. However, there are significant financial and service benefits to doing so. As development has spread out, it has placed greater and greater financial pressure on the municipality. Likewise, it has become operationally difficult to provide services efficiently in many areas. While it is difficult to anticipate the financial impact of unplanned development, the Regional MPS should be able to reduce cost pressure by $250 million over the life of the Plan.

The impact of a future with unplanned growth is ultimately not financial, it is a service impact. The Regional MPS is not a tool to save money. The Regional MPS is a means of creating the communities all across HRM that residents want, with the services they require, at a cost they can afford. By planning for a mix of different settlement patterns all across HRM, the Regional MPS has created a map for the future which provides not only financial stability but which also matches municipal service expansion to new growth areas.