THE CITY OF CALGARY LONG RANGE FINANCIAL PLAN 2011

THE CITY OF CALGARY

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Executive Summary

Sustainability has become a significant focus and offers a pragmatic response to the challenges facing our city. In the municipal context, it is about making our community a better place for current and future generations. It involves considering and addressing the social, economic and environmental impacts of all decisions and actions with regard to planning, policy, strategies, services, operations, approvals and all other City business. In support of this direction, The City has developed a ten year strategic guide for transformation known as the 2020 Sustainability Direction, which establishes a vision and framework for Council's Fiscal Plan for Calgary (Council's Plan).

Citizens expect and value the services provided by The City. Systemic issues related to revenue and funding sources, expenditures pressures, extensive suburban growth, and a tax imbalance have placed considerable pressure on The City's ability to provide services in a financially sustainable manner. Council's Plan recognizes the impediments posed by these systemic issues and proposes a vision for a municipal government that is more citizen-centred, cost-conscious, and innovative. Council's Plan states, as one of its key elements, that existing principles and practices governing municipal finance are unsustainable and must change if Calgary is to maintain and enhance its current financial position. Furthermore, in response to these challenges The City must incorporate a greater emphasis on improvements to efficiency and effectiveness in the delivery of municipal services. The overall intent of this Plan is to ensure that City programs and services can continue to meet citizen needs and expectations and achieve desired outcomes over the long-term.

The City of Calgary has a solid record of incorporating a longer-term* view into its financial documents. Examples include the provision of budget forecasts to Council, the development of the "shadow budget" that showed the longer-term impacts of current decisions and, more recently, in the creation of three-year operating and capital budgets and a five-year capital plan tied to department business plans. The City's first Long Range Financial Plan (LRFP) in 2007 was yet another step in creating a more purposeful approach to long-term financial management.

The LRFP provides a projection of our operating and capital requirements and statement of financial position over the next 10 years. It presents the key financial strategies that will influence the building of a more sustainable long-term financial future. The 10-year projections are founded on a series of assumptions using current economic and demographic data. The assumptions use only information known at the present time and do not include speculation as to future directions of City service levels, debt policies or additional assistance from other orders of governments.

The model estimates The City will face significant annual operating and capital budget shortfalls in the next decade, which cannot be addressed through projected levels of existing revenue sources. The combined cumulative operating and capital revenue and funding deficiency is projected to be approximately $7 billion over the next 10 years. Sensitivity analysis indicates that changes to base assumptions would not materially affect the situation. New or unforeseen spending requirements not currently reflected in the 10-year capital budget system would further increase this shortfall.

* For the purpose of this document, "long-term" is defined as 10 years and beyond.

The LRFP is designed to encourage progress toward the organization's long-term financial goal of sustainability. In order to define strategies and actions for becoming sustainable, as well as assess the degree to which sustainability is being achieved, a clear understanding of financial sustainability is necessary. For the purpose of this document, financial sustainability is defined as:

> "The enduring ability of The City to ensure that it can deliver the level and types of services expected by the community, while proactively assessing and managing associated risks, at acceptable levels of taxation and fees."

The over-arching goal of sustainability is further supported by five main financial goals, including:

- Flexibility: being able to respond to changing circumstances, which may relate to economic, social, environmental or political conditions.
- Efficiency: using public funds in ways that provide the highest level of needed services possible within the amount of funding available.
- Sufficiency: having sufficient resources to support the delivery of services for which The City of Calgary bears responsibility.
- Integration: ensuring the financial constraints under which The City operates are fully considered when engaging in policy-making and decision-making.
- Credibility: achieving financial performance in a way that maintains and enhances public confidence in the municipal corporation.

The five financial goals are further supported through eight strategy areas. These strategies, which will spur actions to both change City approaches and maintain current beneficial practices, include:

- Ensuring adequate funding.
- Achieving diverse sources of funding.
- Managing expenditures.
- Providing for contingencies.
- Using debt strategically.
- Operating with prudent foresight.
- Maintaining sufficient cash flow.
- Promoting and enabling integration.

The initial LRFP was presented to Council in March 2007 in order to improve our long-term view of potential financial status and alternatives. The series of LRFP updates will provide Council with an ongoing, longer-term perspective on The City's financial prospects. The LRFP assumptions will continue to be refined, its projections will build on more customized data and scenarios, and its strategies will continue to be tested by changing circumstance.

1. Introduction

The current financial situation of The City of Calgary reflects a strong financial position, prudent fiscal practices, low residential taxes, solid reserves, high but manageable debt and an AA+ credit rating. All of these factors contribute to The City being in a sound financial position.

Although The City's current financial position is sound there are some systemic and emerging issues that could potentially threaten The City's financial sustainability. Insufficient and inflexible revenue-raising tools to fund expenditures, growth related expenditures exceeding revenues, growing demand to fund future infrastructure, unreliable long-term capital grant funding from other orders of government, a volatile economy, pressure to keep municipal taxes low and over-contribution of taxes to other orders of government are among the significant factors contributing to The City's financial challenges.

Without definitive action to address these factors, The City will become increasingly challenged to provide the services and infrastructure that Calgarians expect and value. The results of a recent public engagement process clearly demonstrate that citizens value City services and do not want to see reductions in these services. While this is very positive it does place an immediate constraint on the options available to The City to address existing and emerging financial issues.

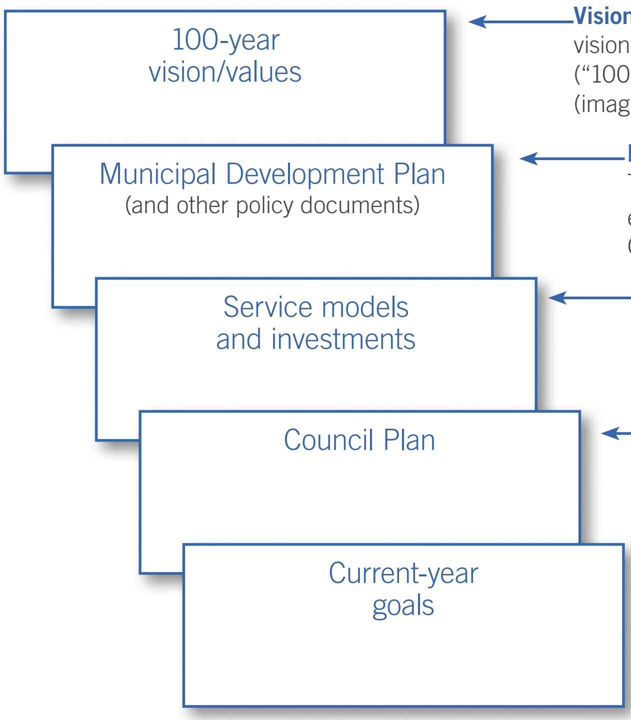
In recognition that the status quo is not a viable option, Council has adopted a Fiscal Plan for The City, the vision of which is to build a municipal government that is more citizen-centred, cost-conscious and innovative. Council's Plan recognizes, as one of its fundamental elements that existing principles and practices governing municipal finance are untenable and must change if Calgary is to maintain and enhance its current financial position. It is necessary to re-evaluate the rules of municipal finance and, where necessary, change them to ensure the sustainability of The City's financial capacity.

This Long Range Financial Plan (LRFP) 2011 Update is another in a series of steps we have taken to first, improve our understanding of our longer-term financial situation and second, to favourably influence The City's long-term financial future.

The report includes five major sections. The first comments on the purpose of, and audience for, Calgary's LRFP. The second section provides background on Calgary's financial state and challenges, to set the development of the LRFP in context. The third section details the 10-year financial projections, describing the key assumptions that went into development of the projections and summarizing the results for the operating budget, capital budget and statement of financial position (balance sheet). The fourth section outlines the key financial goals and strategies that respond to the 10-year projections, as well as an evaluation of the progress being made toward improved financial sustainability, while the last section provides a summary and conclusions about the results and the expected next steps for the LRFP.

Connections to other planning work

The achievement of a sustainable long-term financial situation for The City of Calgary is more than a financial planning exercise. The range and scope of services and physical infrastructure provided by The City requires that planning initiatives be undertaken in many areas and over several time horizons. The City of Calgary is involved in a number of major planning efforts that contribute to its ability to effectively respond to its responsibilities as a municipal government. The City's system of plans is depicted below, starting with the vision for long-term growth and development, continuing through medium-term policy and planning initiatives and finishing with short-term action-oriented plans. These approved plans provide critical linkages to how The City will address pressures affecting citizens, land use, transportation, the environment, infrastructure, partners and fiscal capacity. The LRFP falls within the financial planning/investment layer, which occupies the eight to 10-year timeframe.



Vision layer
vision, values, goals, targets
("100 years" – community generated)
(imagineCALGARY)

Policy layer
Triple Bottom Line view (20 to 30-year timeframe)
e.g. Plan It Calgary (land use and mobility plans), Environment Plan, Economic Development Plan, Calgary Metropolitan Plan, social/cultural plans.

Financial planning/investment layer
(eight to 10-year timeframe) e.g. 2020 Sustainability Direction, Infrastructure Status Report, Long Range Financial Plan, priorities for Transportation (TIIP), Cultural/Parks/Recreational (CPRIIP), Emergency Response (ERIIP), and Corporate Level (CLIIP) infrastructure capital investment.

Priorities layer
Council-driven (two to five-year timeframe)
e.g. Council's Fiscal Plan, multi-year business plans and budgets, Corporate Direction, measurable outcomes.

Accountability layer
deliverables (current year) e.g. 2012 goals: transform municipal government, citizen-centred, cost-conscious, innovative.

These inter-related planning and policy efforts have the potential to significantly impact The City's finances. Consequently, the LRFP can perform a valuable role in both reflecting and anticipating the impact of significant policy and planning initiatives. Here is a brief outline of some significant initiatives.

- **Vision layer** – imagineCALGARY provides a view of a desired Calgary 30 and 100 years from now, drawing heavily on widespread community input. The initial report was completed in 2007. The targets included in the report have influenced the development of business plans across the corporation.
- **Policy layer** – Plan It Calgary draws on the work of imagineCALGARY, producing the Municipal Development Plan, which will set out the land use planning design of the community for the next several decades, and the Calgary Transportation Plan, which will set out the future transportation needs of the city.

  Fair Calgary revises policies regarding access to City services to ensure that Calgary is a socially inclusive, liveable and sustainable city.

  The Calgary Metropolitan Plan includes a comprehensive regional land use plan, governance strategy and principles for regional servicing. This plan is intended to balance the need to protect our regional landscape with the growth of our developed area and the need for regional infrastructure and services in an intentional and proactive way. This Plan was approved by the 15 member municipalities in 2009 and was submitted to the provincial government. Since that time the Calgary Regional Partnership has been working with the government to further re-develop the plan and will re-submit it by the end of 2011.
- **Financial planning/investment layer** – includes the Asset Management Policy which identifies specific principles to manage The City's more than $50 billion in assets focused on the total lifecycle needs of existing and future sustainable infrastructure. This work also pulls together individual capital priority plans such as the infrastructure investment plans for Transportation (TIIP), Culture, Parks and Recreation (CPRIIP), Emergency Response (ERIIP) and Corporate Level (CLIIP). The Asset Management Policy documents The Corporation's commitment to asset management, outlines the guiding principles and elements of asset management and highlights the framework that enables an asset management strategy, objective and plans. In addition, the Infrastructure Status Report is a key document to help Council make informed infrastructure investment decisions.

  The City's 2020 Sustainability Direction is intended to provide a measured, integrated and innovative framework including goals, objectives and strategies to guide decision-making that will promote a sustainable city. The Sustainability Direction is a 10 year strategic guide for transformation which provides The Corporation with a consolidated direction for community well-being, a prosperous economy, a sustainable environment and smart growth and mobility.

  The Long Range Financial Plan is included in this layer. The purpose of the LRFP is to promote awareness of the potential financial challenges facing The City and propose goals and strategies that will guide future actions leading to financial sustainability.
- **Council's Plan layer** – reflects Council's leadership in developing three year priorities including transforming municipal government through innovation, transparency, engagement and being cost-conscious and citizen-centred; and three-year business plans and budgets and subsequent adjustments.

- **Accountability layer** – in addition to the annual goals, Council and the public regularly receive reports to track achievement of Council priorities, goals, strategic results, performance targets and budgets. The completion of the major planning efforts would affect the priorities and accountability layers.

The financial impacts of any future Council decisions associated with these planning initiatives that have not yet been identified will be incorporated into future updates of the LRFP.

City infrastructure reports

Much of the financial challenge facing The City results from growth pressures and the growing demand to fund infrastructure projects. This demand paired with the challenge of unreliable long-term capital funding sources from other orders of government places The City under significant financial stress. The LRFP is one of three periodic City of Calgary documents that consider long-range infrastructure projections, relying on information contained in the 10-year Capital Plan prepared by the various business units. The LRFP projections contain both growth and existing infrastructure but also extend to cover all City operations, including non-infrastructure services, plus overall impacts and strategies. While these documents are related, each has a different focus and target audience.

- **Strategic Growth and Capital Investment (SGCI)** deals specifically with future infrastructure capital requirements related to population growth, including the geographic location of new infrastructure. It is also part of The City's strategy to manage growth, by establishing a framework to inform key decisions in the planning process and ensuring alignment of municipal capital projects related to growth. Strategic Growth is not a policy document but it is a tool to assist in making more informed decisions on coordinating long-term growth.
- **The Infrastructure Status Report (ISR)** includes growth but also deals with the capital and operating requirements of existing infrastructure, including condition and maintenance costs. The City of Calgary is challenged to balance the capital investment required to support growth while funding maintenance and upgrades of existing infrastructure. The ISR is a key document to help Council make informed infrastructure investment decisions. It provides information on infrastructure condition in order to ensure that assets maintain the ability to deliver required services to the citizens of Calgary. The ISR is a key part of the integrated framework of processes, tools and documents to enable The City to implement effective asset management practices.

Although the reports offer different perspectives and approaches, each deals with different aspects of City infrastructure requirements over a 10-year period and assists in providing context regarding the financial challenges facing The City.

Purpose

The City of Calgary has a rich history of corporate planning efforts exemplified most recently by The 2020 Sustainability Direction, a 10 year strategic guide for transformation that will promote a consolidated direction for community well-being, a prosperous economy, sustainable environment and smart growth and mobility. Starting in 2011 with this update of the LRFP, the longer term view of our financial efforts will be put into the context of, and support, the principles of the Sustainability Direction.

In the past several years, The City devoted a more concerted effort to financial planning. For example:

- A three-year "shadow budget" was developed, beginning in 2003, as a way to demonstrate the longer-term impacts of current Council budget decisions.
- The building of an integrated business planning and budgeting process, beginning with the 2006-2008 cycle, featured Council approval of three-year plans and operating budgets, followed by annual approval of adjustments to those plans and budgets.
- Continuation of this practice for the 2012-2014 cycle, including a public engagement process for a combined facilitated review of core services and the business planning and budget coordination process, which gathered information from citizens, employees and Council about the most valued City services and priorities, and how budget dollars should be allocated now and in the future.
- The long-standing practice of building a five-year capital plan to complement each three-year capital budget for Council approval is now tied to corporate infrastructure status reports.
- Continued enhancement of the capital budget process with initiatives to coordinate investment priority lists and identify opportunities to prioritize capital project spending and to accommodate and manage growth.
- Inclusion of the operating impacts of new capital projects within the capital budget and in the annual adjustments to the operating budget submitted for Council's approval.
- Continued evolution of the Infrastructure Status Report to improve the process through which it determines financial implications of providing new, and maintaining existing infrastructure.
- Development and update of the Long Range Financial Plan extended The City's financial planning horizon by projecting costs and revenues for a 10-year period, identifying potential funding gaps and providing goals and strategies aimed at improving financial sustainability.

The LRFP 2011 Update is designed to meet the following eight purposes:

- To support and reflect Council's Plan to build a municipal government that is citizen-centred, cost-conscious, innovative and efficient.
- To update the assumptions and projections presented in previous plans.
- To continue building awareness of the results of 10-year projections of current operating and capital spending and funding levels.
- To assist The City in determining the extent of its financial challenges.
- To reconfirm the key financial goals and strategies that should guide future planning.
- To spur the development of actions in department business plans that respond to the long-term strategies.
- To provide an ongoing basis for negotiations with the other orders of government on the equitable sharing of resources.
- To evaluate progress toward improving financial sustainability.

This document follows the same general format as the original LRFP and subsequent updates for consistency and ease of comparison.

Audience

The LRFP 2011 Update both sets a financial context for other planning efforts underway in the organization and provides another building block for the creation of a more sustainable financial future for The City. As such, it is designed primarily for use by the following groups:

- City Council
- senior administration
- those involved in other major corporate planning initiatives
- the finance, business planning and asset management networks within The City of Calgary
- intergovernmental affairs contacts

The LRFP 2011 Update is available as basic information needed to help prepare plans and strategies for the future. Its usefulness is in providing a long-term financial perspective and a better sense of where current trends would take this organization. Its proposed goals and strategies guide the development of business plans designed to take action to improve The City's financial picture.

The LRFP does not present a 10-year budget for The City of Calgary. It is not a document to be "approved"; it is a view of a possible future to inform and act upon. Neither is it a true forecast, in the sense of providing a probable outlook or best estimate on what the next decade will bring.

2. Background

Key challenges and trends

The current financial situation of The City reflects a strong financial position, prudent fiscal practices, low residential taxes, solid reserves, high but manageable debt and an AA+ credit rating. These factors contribute to The City being in a sound financial position.

Although The City's current financial position is sound there are systemic and emerging issues that threaten The City's financial sustainability. Insufficient and inflexible revenue-raising tools to fund expenditures, growth related expenditures exceeding revenues, growing demand to fund future infrastructure, unreliable long-term capital grant funding, a volatile economy, pressure to keep municipal taxes low, over-contribution of taxes to other orders of government, shifting demographics, and social and environmental issues are among the significant factors contributing to The City's financial challenges.

Each of the following issues poses a significant hurdle to the overall goal of long-term financial sustainability:

- **Limited revenue sources.** Although The City of Calgary is responsible for providing a wide range of essential services that citizens expect and value, it must rely on only a few limited sources of revenue. The City's revenue sources are not broad enough and the amount they provide is inadequate to meet expenditures. Furthermore, the primary revenue source available to The City, property tax, is not sensitive to economic growth.

- **Costs of new growth.** The cost of supplying and maintaining infrastructure and associated services to support new growth places considerable demands on City budgets. Because of the long lead times required to plan and build municipal infrastructure, The City must anticipate growth and plan, finance and build required infrastructure before the tax base exists to contribute revenue toward these costs. This places additional stress on municipal finances. The rate of suburban expansion presents additional challenges for The City since suburban development requires new infrastructure and upgrades to existing infrastructure that are more costly than redevelopment in existing areas of the city. Furthermore, infrastructure required to support new growth also includes on-going, long-term operating costs that contribute to The City's financial commitments.

- **On-going infrastructure requirements.** The City is challenged to balance demand for the capital investment necessary to support growth while also ensuring the continued maintenance and upgrades of infrastructure already in service. The City's Infrastructure Status Report shows that over the next 10 years The City will require significant additional investment to fund infrastructure growth and maintenance. When complete, this infrastructure will continue to require a financial commitment from The City in the form of operating expenditures further adding to the financial burden.

- **Unreliable long-term capital grant funding from other orders of government.** The City does not have sufficient fiscal capacity to provide a level of infrastructure necessary to meet current demands and accommodate future growth and must rely on transfer payments that can be changed at the discretion of other orders of government, or incur additional debt. This creates uncertainty in financial planning due to potential unexpected changes to funding caused by the changing priorities of other orders of government. Furthermore, The City must continue to fund associated on-going operating expenditures from limited and largely inflexible sources of revenue.
- **Volatile economy.** Calgary is challenged by a cyclical economy. The city has repeatedly experienced periods of rapid economic and population growth followed by periods of stagnation or even contraction. This presents challenges in establishing stable levels of services and revenue.
- **Tax resistance.** Although Calgary's residential property taxes are low on the Canadian scale, there is considerable pressure to control tax rate increases because property tax is highly visible. Increases in property tax have politically acceptable limits, even if a significant portion of the increase can be attributed to an external factor such as inflation. The key to managing this is ensuring that taxpayers perceive that they are receiving fair and prudent value for their tax dollars.
- **Fiscal imbalance.** Taxpayers in Calgary over-contribute to the Federal and Provincial governments. This means that the taxes and other payments going to these orders of government exceed the benefits received by Calgarians. This leaves local government with less than adequate revenue to fund its spending responsibilities and requires the use of debt to bridge the gap. This places further stress on The City's financial position.
- **Shifting demographics:**
  - **Population.** While Calgary has a relatively young population the number of older Calgarians will continue to increase, which will fuel the demand for age-sensitive City services.
  - **Workforce.** An anticipated wave of retirements in the coming years will create a loss of leadership and knowledge that will need to be managed in order to sustain City services. In addition, a tightening labour market will reinforce the need to remain competitive in salary and benefits, which will add to the costs of service provision.
- **Social and environmental issues.** In times of both economic prosperity and slowdown and recovery, Calgary faces challenges from related social issues, such as different types of crime, more homelessness and greater incidence of poverty. Maintaining the quality of the environment also has become a challenge in a large, growing city.

Taken together, the sum of the issues is greater than its parts: a resource-intensive operation with static revenue sources; growth-related expenditures which exceed available revenue; increasing demand for both new infrastructure and prudent management of existing assets; unreliable and often conditional long-term capital grant funding; a resource-based economy prone to rapid swings; considerable pressure to control tax rate increases; a fiscal imbalance between the orders of government; a relatively young, diverse population which values and expects a high quality of local government service; and a major employer facing competing demands for skilled staff and a web of services to provide to a market where sheer size is creating diseconomies of scale. The following passage illustrates one of many significant challenges facing The City:

"The Canadian and Alberta governments have experienced increased financial prosperity over the 1988-2007 period. This is in contrast to the financial situation in large urban municipalities such as The City of Calgary, where revenue growth was not enough to take care of their increasing responsibilities. The success of the Government of Canada and the Government of Alberta in improving their financial position over the last ten years came largely from the contributions of citizens in leading economic regions such as Calgary. Those regions are the urban areas where a majority of Canada's working age population and employed labour force live and work, and where most of the country's economic activity occurs." The City of Calgary, *A Case of Fiscal Imbalance: the Calgary Experience*, November 2010

Calgary in the Canadian context

Some of the challenges Calgary faces are fairly common to all of Canada's major cities. There have been numerous studies in the last decade on the difficulties cities encounter in providing for an expanding populace within constrained resources.

"...The ability of western Canada's cities to meet these huge infrastructure requirements is hampered by a singular and heavy reliance on the property tax. Real per capita growth in property tax revenue is well below growth in tax revenues seen federally and provincially, and property tax revenues relative to personal disposable incomes and GDP are at some of the lowest levels ever seen. The attendant lack of diversity in tax tools constitutes a serious disadvantage when it comes to infrastructure investment. To help place our cities on a more firm fiscal foundation, reforms are needed that include the introduction of new tax tools." Canada West Foundation, *The Penny Tax*, April 2011

"Unlike sales or income taxes, the property tax base does not grow as the economy grows, which constrains the City's funding base compared with other orders of government. Toronto's economic health anchors the entire region and the Province benefits through the City's tax revenue. Toronto competes with large U.S. cities that have access to sales and income taxes and risks relative decline without comparable revenue base. The participation in economic/tax growth would motivate greater focus on the City's broad economic development role by other orders of government. **This is a financing tool that all cities in Canada should have to eliminate structural shortfalls and ensure sustainable long term financing (emphasis added).**" The City of Toronto, *2010 Corporate Report*, March 2010.

Thus, Calgary's LRFP identifies similar pressures faced by other cities and corresponds to similar long range financial planning that has been done and is continuing in such major Canadian cities as Toronto, Edmonton, Ottawa and Winnipeg.

In response to the common pressures facing Canadian cities, The City of Calgary has collaborated with other municipalities and organizations to advocate positions in support of municipal concerns.

These advocacy initiatives enable The City of Calgary to build an important network of government-to-government relationships, and to highlight the specific needs of Calgary. Continued efforts in this arena are a key element in The City's efforts to maintain and enhance financial sustainability.

The City of Calgary's current financial condition

By any measure, The City of Calgary, despite its considerable future challenges, is currently on a solid financial footing. Its reputation for sound financial management within a growing local economy has resulted in continued strong credit ratings of AA (high) from the Dominion Bond Rating Service and AA+ from Standard and Poor's. The City's three-year approval of business plans and capital and operating budgets is unique among large Canadian cities and offers a degree of foresight and financial stability that is complemented by a growing tax base, diversified and highly liquid investments and substantial reserves.

The organization's principal financial characteristics (generally taken from The City of Calgary's 2010 Annual Report unless otherwise noted) are summed up as follows:

- **Size:** a three-year operating budget of $7.6 billion over 2012-2014 and a five-year capital plan of $5.5 billion for 2012-2016.
- **Surplus:** there was an operating budget surplus of less than one per cent in 2010. This number was lower in previous years.
- **Staff:** The City had approximately 15,000 full-time equivalents (FTEs) at the end of 2010. This translates into approximately 14 FTEs per 1,000 citizens, an increase from 12.5 in 2001 due to increased service requirements associated with a growing city. The number is below that for several major Canadian municipalities and has been for the last decade.
- **Taxes:** average municipal residential property taxes of $1,174 in 2010 based on the median assessment of $374,000 for a residential property. According to a City of Edmonton survey dated April 2011, Calgary has the lowest residential municipal property taxes and the fourth lowest combined municipal property tax and utility charges for a sample house among the 20 largest cities in Canada.
- **Assets:** total assets (book value) were over $16 billion in the annual financial statements for the end of 2010, including the net value of ENMAX, The City's wholly-owned electrical utility. Over the past five years, City assets have grown at a faster rate than liabilities, to a net asset position of more than $11.3 billion at year-end 2010. (This figure reflects the new reporting requirements of the Public Sector Accounting Board).
- **Debt:** total debt (excluding ENMAX) is approximately $2.9 billion, of which 15 per cent is tax-supported and the remainder is self-supported. The tax-supported debt per capita is about $407 and debt servicing charges make up approximately four per cent of tax-supported gross expenditures (compared to a City policy of a 10 per cent limit).
- **Reserves:** total reserves of more than $1 billion as of the end of 2010, the majority of which are allocated to specific future projects. The unallocated Fiscal Stability Reserve, The City's contingency fund, had a balance of approximately $225 million at the end of 2010.

The City's assets are currently stated at more than $16 billion and its net assets at more than $11.3 billion. Under current accounting rules (Public Sector Accounting Board) most of the tax-supported portion does have depreciation applied to it. At the same time, it does not reflect replacement value currently estimated at over $50 billion.

In 2009, the most significant accounting change in decades came into effect, requiring municipal governments to amortize (depreciate) capital assets over their useful lives. The requirement to report asset amortization currently applies only to actual results and not to budgets and projections. Because the requirement is relatively recent and there is a lack of history upon which to base a projection, amortization on tax-supported assets has not been included in The City's budgets for 2012 to 2014 and is therefore not included in the LRFP projections. The recovery of amortization expense for total City assets is not currently factored into property tax rates. Given The City's considerable asset base, the amount of amortization expense recognized is significant. Amortization expense recognized in 2010 was approximately $400 million and is projected to be approximately $600 million by 2021. The decision to include asset amortization in projections will be reassessed with each future update.

The medium-term economic and social outlook for Calgary is for gradual recovery following the current economic downturn. Calgary has outperformed the Alberta and Canadian economies over the last 10 years, and Calgary and Alberta are expected to recover at a modest pace in 2011 following the sharp economic contraction of 2008-2009. Alberta has one of the lowest unemployment rates in the nation, the highest personal income and personal disposable income, and the lowest combined provincial and municipal tax load. The City of Calgary's Corporate Economics Section's forecast for Calgary's economy for the next ten years anticipates:

- Population growth averaging 1.4 per cent per year through 2021.
- Unemployment rates declining from 7.0 per cent in 2010 to 4.0 per cent in 2021.
- A gradual decline in inflation from 2.2 per cent in 2011 to 2.0 per cent by 2021.
- Increasing annual new home starts from 6,400 in 2011 to 7,300 in 2021.

Although The City's current financial situation is sound there are some existing and emerging issues that need to be considered when evaluating The City's long-term financial sustainability. The City is responsible for providing a wide range of services expected and valued by citizens but must do so with only a few limited sources of revenue. Furthermore, most of these revenue sources, including property tax, are not sensitive to economic growth. Tax revenues account for approximately 50 per cent of The City's total revenue. Other sources of revenue such as sales of goods and services are more volatile and do not have mechanisms in place to ensure adequate growth, creating a structural fiscal problem for The City whereby growth in expenditures consistently outpaces growth in revenues.

While Calgary's residential property taxes are low on the Canadian scale, there is considerable pressure to control tax rate increases. Service expansion pressures and increasingly significant infrastructure expenditures are expected to continue to drive up operating expenses and debt levels over the medium term. A growing demand to fund future infrastructure projects, combined with the challenge of unreliable long-term grant funding sources has also been identified as an area of concern. The City's level of debt will grow in the short term. However, according to Dominion Bond Rating Service, given the self-supporting nature of the majority of the debt, the increased debt burden should still remain manageable. In addition, Calgary will benefit from low-cost financing from the Alberta Capital Financing Authority and substantial liquid reserves which are in excess of anticipated incremental borrowing requirements. These factors will provide resilience to The City's financial profile.

3. Long-range projections

The City is facing significant financial challenges. The state of municipal finance is such that opportunities to raise additional revenue and funding from new or existing sources are extremely limited. The City's main source of revenue is derived from property tax, which has proven to be inflexible and inelastic. Other internal sources of revenue such as the business tax and sales of goods and services also present limited growth potential. Funding from other orders of government is at their discretion and is subject to change or elimination as provincial and federal agendas evolve.

Meeting citizens' service expectations has also placed stress on City finances. Increasing existing levels of service, introducing new services, meeting the demands of growth and responding to inflationary pressures all contribute relentlessly to a profile of expenditures that exceeds available revenue.

The foundation for understanding the extent of The City's financial challenges is a projection of its financial situation 10 years into the future. The projections demonstrate the adequacy of revenue and funding to cover expenditures. A multi-year financial projection is an essential tool for long-term planning. The purpose of a multi-year projection is to:

- Illustrate the relative magnitude of the financial challenges facing The City.
- Stimulate discussion on how to address the general trends they reveal.
- Assist in planning strategy and actions that will contribute to The City's long-term financial sustainability.

The operating projection is based on providing the same kinds of services currently provided and spending the same amount per capita (adjusted for forecasted inflation) to provide those services. This would be equivalent to maintaining the existing per capita resources and efficiency for each current City service. This approach to developing financial projections does present some limitations. For example, projections prepared under this methodology cannot anticipate or adequately capture the costs of new growth nor do they reflect any potential financial benefits that could be realized through improvements in the efficiency with which The City delivers services. There are potential risks associated with this simplified approach that could result in inaccuracies in the projections. However, it is assumed that any potential inaccuracies would not be of significant materiality and, therefore, would not change the direction or the magnitude of the projections.

It is also important to remember that the inflationary pressures to which The City is exposed are considerably different to those faced by individual consumers. City expenditures are comprised primarily of salaries, wages, benefits and material costs, all of which are subject to different dynamics than the food, housing and transportations costs reported in the news. This subjects City expenditures to a degree of financial strain that may not typically be experienced by retail consumers.

The capital projection is based on maintaining and extending infrastructure to serve the forecasted population according to the 10-year capital plan as well as carrying out the not-funded projects included in the capital budgeting system.

The base projections developed for this report use demographic and economic forecasts such as population growth, municipal service cost inflation and Consumer Price Index (CPI), and commodity prices. Projections of City operating expenditures and revenues differ from forecasts in that the intent of projection does not to try to determine if or when certain service changes happen. Rather, these numbers only project how The City's financial state would change if the current level of resources (the services and infrastructure expenditures reflected in the business plans and budgets approved for 2012-2014) were to continue relatively unchanged from 2015-2021.

The projections developed for this report assume a 10 year period of relatively stable and predictable growth. In reality, Calgary is challenged by a cyclical and volatile economy. Periods of rapid economic and population growth are often followed by periods of contraction or stagnation. Both extremes present unique challenges to The City's ability to manage its financial situation and fulfill service and infrastructure commitments.

Robust economic growth often results in record population growth as people are attracted to the opportunities that it presents. This places immediate pressure on municipal finances as The City is challenged to provide services and infrastructure necessary to respond to growth with constrained and inelastic sources of revenue. At the same time, higher rates of inflation and competition for workers during periods of high economic growth tend to put significant pressure on wages.

Economic contraction places an equal strain on municipal finances. The City is still obligated to provide mandated and expected levels of service and infrastructure at a time when revenues can face pressure. Components of municipal revenue are sensitive to factors such as commodity costs and development activity which respond to general economic conditions. The 10-year projections contained in this update of The City's LRFP can be expected to be refined with each successive update. Improved projections will result from obtaining details about decisions on planning projects currently underway and improving long-range financial modelling capabilities.

Operating projections in the 10-year model

The 10-year operating budget projection model is based on the proposed 2012-2014 operating budget and projects seven years beyond it, including impacts of population growth. It shows what The City's financial situation could look like in 10 years if the environment were to unfold as forecasted and The City were to continue providing the current per capita resources for services in the same way as it does now.

Capital projections

In addition to its operating projection, the 10-year model projects capital expenditures and funding. It is based on all funded and unfunded capital programs identified by City Business Units. It shows over the next 10 years that currently available funding sources will not support all identified capital programs.

Statement of financial position projection

The statement of financial position links the operating and capital projections to show what The City's assets and liabilities could look like 10 years from now. When the operating and capital projections indicate revenues and/or funding would be less than expenditures for one or more years, the projected statement of financial position will not be completely realistic. Because the operating budget will essentially be balanced every year, this cumulative gap can be viewed as the indicative cost of service declines. The statement is useful to broadly observe the cumulative changes in The City's financial position over the 10-year period.

Assumptions

The results of long-range financial projections are totally dependent on the assumptions made about such things as population growth, the economy (including inflation rates), the services provided and changes to revenues and expenditures. The assumptions chosen for the base projection include:

- 2012 to 2014 operating budgets reviewed by Council for the purpose of setting indicative tax rates for these periods.
- Capital projects already included in the capital budget system (funded and not funded).
- Population growth and inflation forecasts gathered from respected sources (The City of Calgary Corporate Economics group; the Conference Board of Canada).
- Moderate revenue growth.

The detailed assumptions shown in Appendix 2 provide a more complete basis for the projections, but some assumptions worth drawing attention to include:

- **Operating expense projections** are developed by applying a series of demographic and economic factors and inflators to currently approved budget data. For example, budget line items such as property tax and licence and permit revenue are projected to grow by a compound rate of inflation and population growth. Other line items which are not sensitive to population growth, such as grants from senior orders of government, are assumed to grow at a rate of inflation only.

  This simplified approach to projecting operating expense assumes that the same kinds of services and the same level of service will continue to be provided into the future. These numbers only project how The City's financial state would change if the current level of resources were to continue relatively unchanged through the projection period.

  This approach to operating projections presents limitations. These projections do not intend to determine whether and when certain service changes could happen and what the financial consequences could be. Projections developed in this manner cannot adequately capture such drivers as the potential costs of new growth and development, nor can they reflect the financial consequences of changes in the efficiency with which City services are delivered. To address these limitations scenarios and sensitivities are considered to assist in evaluating the stability of projections and demonstrate the impact of alternative assumptions on City finances.

Despite the potential limitations associated with this approach to operating projections, the results support the fact that The City's financial capacity is challenged by a number of systemic issues. Insufficient and inflexible revenue-raising tools to fund expenditures and growth-related expenditures exceeding revenues are two significant factors contributing to The City's financial challenges.

- **Future infrastructure capital maintenance and growth requirements** that have no identified funding source are dealt with in the projections through the assumption that not-funded projects in the capital budget system will require funding over the next 10 years. Also, there are capital funds over the 10 years not yet allocated; these unallocated funds are considered to be applied to the group of not-funded projects to determine the net shortfall.

  If additional projects arise that are not currently in the capital budget system, the capital funding gap would increase. Additionally, the 2010 Infrastructure Status Report (ISR) indicated large, not-funded infrastructure operating requirements averaging approximately $75 – $100 million per year that are not included in the operating projection. Funding infrastructure growth and maintenance is an area requiring strategies and decisions that has significant potential to affect long-term financial requirements. Council decisions based on these recommendations and financial considerations, and those discussed in Section 4 of this document, will improve the overall 10-year capital projections and the infrastructure operating maintenance component of the 10-year operating projections.

  These capital projections illustrate that The City continues to face structural financial issues that impact its ability to effectively provide infrastructure expected and valued by Calgarians. The City is challenged to balance demand for the capital investment necessary to support growth while also ensuring continued maintenance and upgrades of infrastructure already in service. To further compound the situation, The City does not have sufficient fiscal capacity to provide a level of infrastructure necessary to meet current demands and accommodate future growth and must rely on transfer payments that can be changed at the discretion of other orders of government.

- **Maintaining expenditures** for each service at a constant number of dollars per capita will provide a fixed level of service.

  It seems reasonable to expect that if expenditures (adjusted for inflation) increase at the same rate as population growth, then service levels will remain constant. However, any services that are affected by declining asset condition, a general policy to increase the service level, or the increasing complexity of a larger city (such as longer travel distances, more traffic congestion, and/or more social, environmental or legal issues) could require more time and cost to provide the same service. While additional efficiencies may help to alleviate to some extent such potential challenges, the provision of some services might not be able to be maintained at existing service levels over a 10-year period. Failing to realise such efficiencies could result in significant tax rates increases to ensure that The City can continue to provide the services that citizens expect and value.

This highlights the challenges facing The City resulting from insufficient and inflexible revenue-raising tools. Growth in expenditures is projected to significantly outpace growth in revenue resulting in a funding gap. Section 4 of this document discusses strategies and actions available to The City to address this potential shortfall.

- **The rate of inflation** on goods and services purchased by The City will be approximated by a combination of the projected Calgary CPI or Municipal Price Index (MPI), Conference Board of Canada forecasts and corporate estimates for specific components, and by Calgary CPI or MPI thereafter.

  The assumption that most City costs will increase at the rate of CPI inflation for at least the last five years of the projection (with limited exceptions such as employee benefits) is worth noting. Clearly, The City's basket of goods and services purchased is different than the purchases used as a basis for the CPI calculation. Over the past 10 years, The City's inflation rate has been consistently higher than the CPI. However, over a 15-year time span, the two rates are close. In recognition of the unique profile of goods and services consumed by The City, a Municipal Price Index (MPI) has been developed and is applied to certain line items in the projections. The purchasing patterns of The City (which emphasize labour costs, materials and equipment) are significantly different to household purchases (such as food, shelter and transportation), which constitute CPI. A combination of MPI and population growth is applied to budget line items such as property tax revenue, licences and permits revenue and internal recoveries to develop projections.

The base assumptions exclude such items as:

- Possible impacts of planning and policy projects being formulated but not yet approved or for which the impact has yet to be determined (e.g. Municipal Development Plan and Calgary Transportation Plan).
- Additional tax-supported debt for the seven years projected beyond the approved 2014 budget.
- Potential new services not approved for implementation by Council (e.g. curbside organics recycling).
- Potential capital projects that are not currently in the capital budget system and may be brought to Council in the future, such as additional funding for the South-East LRT. Such items are not yet included in the 10-year capital projection, so they could result in changes to the projection in future updates.
- Potential business plan and budget adjustments for 2012-2014.

Because the assumptions affect the projections so much, it is important to understand what the assumptions are and how changes to them could alter the outcome. As a result, the report includes examination of selected sensitivities.

Projections

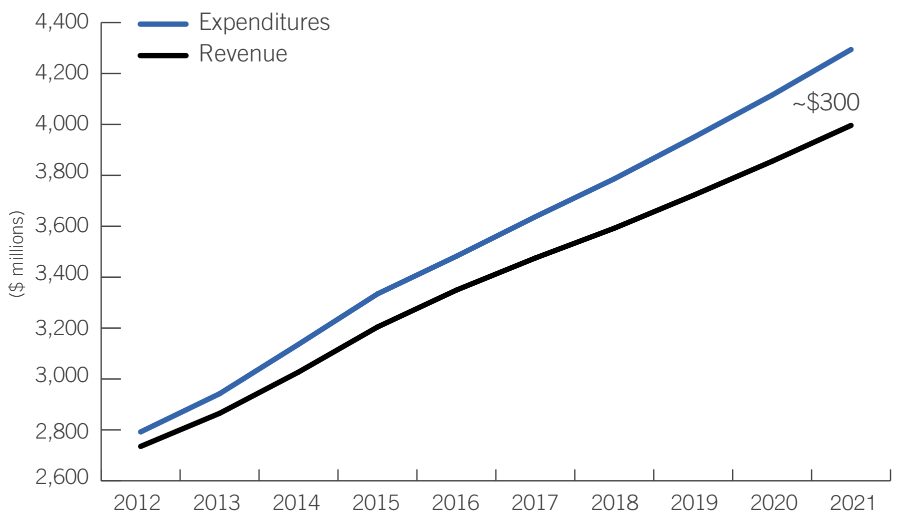
As indicated previously, there are many potential circumstances that could occur within the short to medium term that would affect the base 10-year projections for operating and capital. The details of Council decisions on planning policies and new and existing services and/or infrastructure will certainly lead to changes when future LRFP updates are prepared.

The base projections included here show the kind of financial sustainability issues The City could face if the status quo as budgeted for 2014 is extended out to 2021. The projections highlight the existing and emerging issues that impose stress upon The City's financial capacity. Insufficient and inflexible revenue-raising tools to fund expenditures; growth related expenditures exceeding revenues; growing demand to fund future infrastructure; unreliable long-term capital grant funding from other orders of government; a volatile economy; pressure to keep municipal taxes low; over-contribution of taxes to other orders of government; and shifting demographics are among the significant factors contributing to The City's financial challenges. It is clear The City can not continue to do the same things in the same way.

Operating projection

Although the operating projection includes the assumption that the property tax base increases proportionally to forecasted population growth, and rates increase by the projected City of Calgary municipal price index (which reflects the projected inflationary increases in The City's operating expenditures), a gap appears between revenues and expenses in the first projected year (2012) and widens until the last year (2021), as shown in Chart 1.

Chart 1
Projected operating revenue and expenditures/net transfers to reserves 2012 – 2021



The revenue shortfall charted above is based on providing current levels of resources, and will vary from projections that include other assumptions such as catching up on deficient service levels or adding new service. The total annual operating funding shortfall reaches approximately $300 million by 2021. These results further emphasize the magnitude of the systemic fiscal problems facing The City. Lack of access to diverse and growth-sensitive sources of revenue results in a significant shortfall to adequately cover expenditures required to provide services expected and valued by citizens.

The information presented in the above graph assumes a budget shortfall at the end of 2014 of approximately $108 million. Assuming that this gap is eliminated through the current 2012-2014 budget would result in a revised gap at the end of 2021 of approximately $150 million. This would assume different levels of service than those currently contemplated in the existing operating projections.

A table showing sample years of the 10-year operating projection is included as Appendix 3.

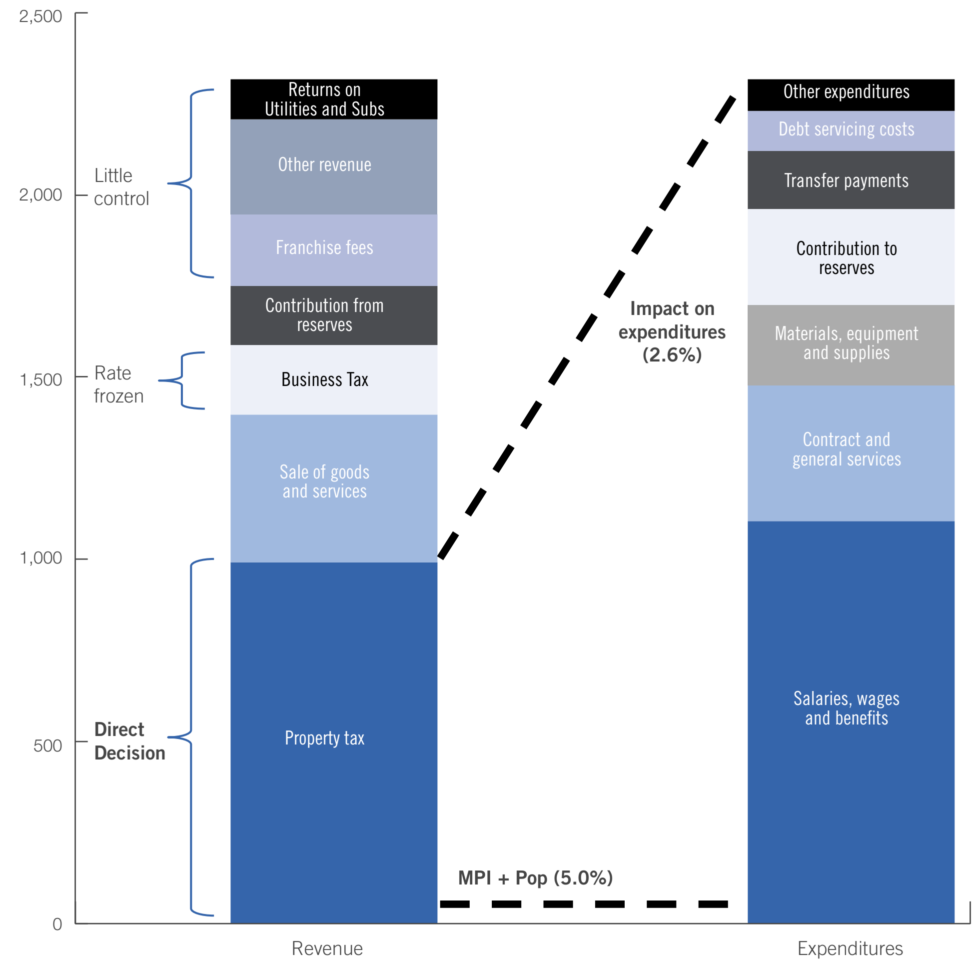
The operating gap emerges largely because the property tax is the only revenue source that is fully controllable (within the constraint of public acceptability), but only makes up less than half of the revenue to support operating expenditures. The remaining revenues cannot be increased simply through Council decisions, as they are impacted by external factors and typically do not grow at the same rate as The City's expenditures. None of these revenues grow proportionately to economic growth on a sustained basis. Based on analysis of historical trends the following revenue assumptions have been identified as contributing to the gap:

- Some revenues do not increase (e.g. dividend contributions to operations).
- Some revenues increase with population or inflation but not both (business tax, Provincial policing grant).
- User fee volumes increase at levels lower than population growth rate (rates increase equal to CPI rate increase).

The contribution from each major revenue source is graphed below in Chart 2, showing the proportion derived from each source. The chart illustrates the structural fiscal problem that faces The City. Property tax revenue accounts for approximately 50 per cent of The City's total revenue. Other sources of revenue such as dividends, business tax and franchise fees are largely fixed, creating a structural fiscal problem for The City whereby growth in expenditures consistently outpaces growth in revenues.

Within the projections, no operating impacts are assumed for potential increases to travel distances, congestion and service complexity related to city growth. There is also no allowance for deterioration of an increasing infrastructure base (e.g. roadways) or general policies that imply increasing levels of service (e.g. the CTP's goal for increasing public transit service hours per capita).

Chart 2
2011 Revenue and expenditures



The base operating projections do not specifically consider the impact of any potential changes to the efficiency with which City services are delivered, although The City will introduce zero-based reviews (ZBR) of City services. This is an examination of all aspects of an existing service, including scope, service level, alignment to long-term policy goals, and potential efficiencies in the way services are delivered. A phased approach to implementing ZBRs is being proposed which will balance the need for review with cost, organizational capacity and citizens' ongoing expectations for quality services. This could impact future operating projections and the effects, if any, will be reflected in future updates.

The projected operating gap for 2021 is approximately $300 million, whereas the 2009 LRFP update projected a gap of approximately $200 million for 2019. This illustrates that The City faces on-going challenges as the operating gap continues to be of the same magnitude and direction from one update to the next, when differences in timing are considered.

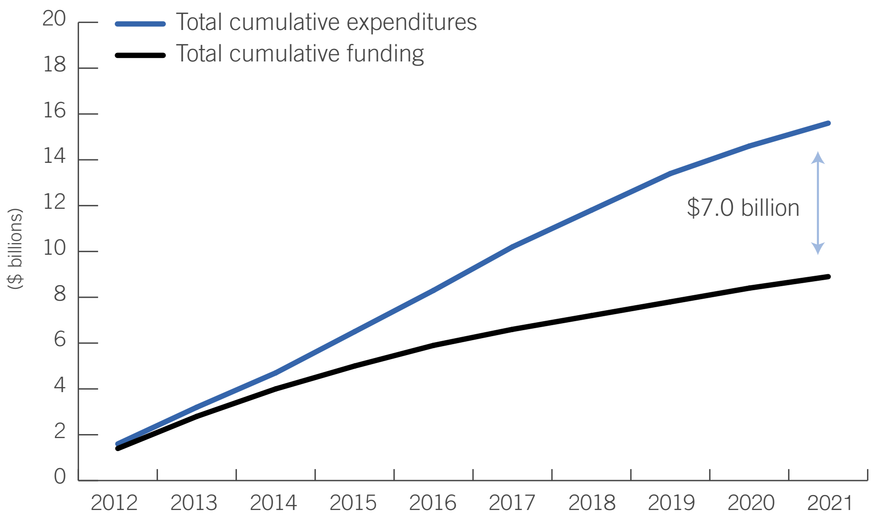
Closing the gap with additional property taxes would require additional rate increases averaging two and one-half per cent each year above the City of Calgary municipal price index forecasts already assumed in the model from 2015 – 2021. The following chapter on Financial Goals and Strategies outlines other ways of reducing the gap.

Capital projection

The capital projections are based on all projects included in The City's ten year capital plan. This includes projects for which a source of funding exists or has been identified (funded capital). All projected funds are identified by their source. The projections also include those projects for which no source of funding or potential funding exists (unfunded capital). The capital gap that is referenced throughout this document comprises unfunded capital projects. The funded capital also includes debt-financed projects. Debt is projected to increase substantially over the projection period. In some cases (i.e. Municipal Sustainability Initiative (MSI) bridge financing) the funding source for the debt is future capital grants and is therefore reflected in the graph through the timing of the funding. The remainder of the debt is funded through operating revenues; therefore the debt servicing costs are reflected in the operating projections. An increase in this type of debt to close the capital gap would result in an increase in the operating gap.

The City is subject to limits on the amount of debt and debt servicing costs it can incur. The debt limit is calculated at 2 times revenue (as defined in Debt Limit Regulation 255/2000) and the debt service limit is calculated at 0.35 times revenue. These limits are guidelines established by the Minister of Municipal Affairs to identify municipalities which could be at financial risk if further debt is incurred. At the end of 2010, Calgary was comfortably within both limits.

Chart 3
Projected cumulative capital funding and expenditures 2012 – 2021



Additional funding for municipalities has been committed to by other orders of government, including the MSI by the Province of Alberta. While these funds support spending to meet critical requirements, they do not provide enough funds to cover all basic infrastructure needs and are not under municipal control to ensure sustainability. In fact, some MSI funding has been delayed as provincial revenues have declined.

Chart 3 shows projected funding and expenditures on a cumulative basis.

The total capital funding identified for the 10 years amounts to $8.3 billion, while the projected capital project requirement is $15.4 billion, leaving a cumulative gap of $7 billion in 2021 (not including any projects and upgrades not currently in the capital budget system). A table showing the 10- year capital projection is included as Appendix 4. Examples of capital projects that have been identified, for which no funding currently exists include the South-East LRT and the redevelopment of the Glenmore and Foothills athletic parks.

Statement of financial position projection

A statement of financial position (SFP) is intended to present the assets, liabilities and net position (equity) of an organization at a given point in time. An SFP projection can be found as Appendix 5 to this document. The projected SFP illustrates that despite the current and future utilization of debt as one of several sources to finance infrastructure, The City will remain chronically underfunded. While debt is projected to increase substantially over the projection period, The City will still face a significant backlog of infrastructure projects for which no source of funding exists or has been identified.

The operating and capital base assumptions result in a projected 2021 SFP which illustrates the overall shortage of operating and capital funding will be in excess of $7 billion over the next 10 years as a result of continuing to provide existing services and identified infrastructure. In the base projections, assets would reach about $26 billion and the projected growth in utility debt would result in a debt balance approaching $4 billion.

Sensitivities

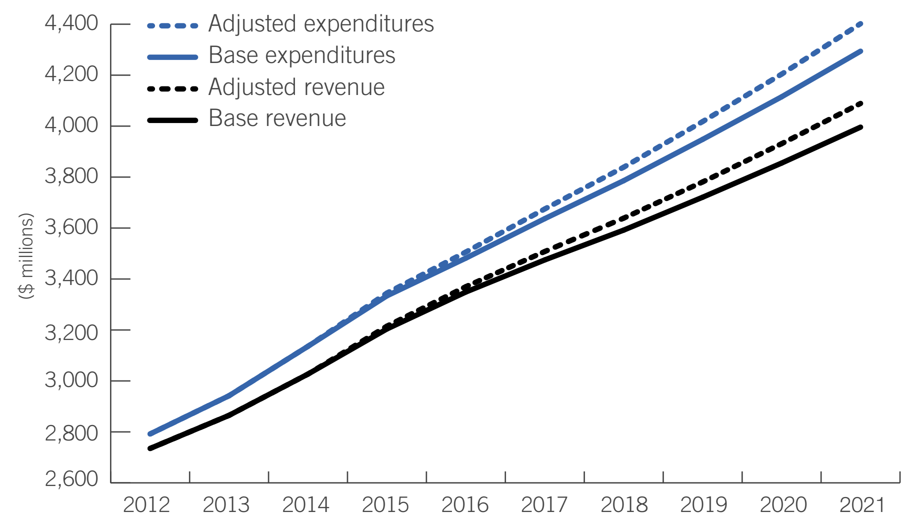
Changes to individual assumptions can change the projections. The 10-year models have been run with changes to the assumptions about population growth rates and inflationary increase rates to see how much difference it makes to the projected gaps.

Population growth rates

To measure population growth rate sensitivity, the forecasted rates were increased by 0.5 per cent per year from 2015-2021. This would result in the operating budget gap increasing by approximately $20 million to a total of $320 million in 2021 as shown in Chart 4. The capital gap would only increase if additional projects were indentified.

An additional sensitivity was created to assess population growth sensitivity in which population growth is assumed to be zero for the period 2015 to 2021. This would result in the operating budget gap decreasing by $40 million from approximately $300 million to $260 million.

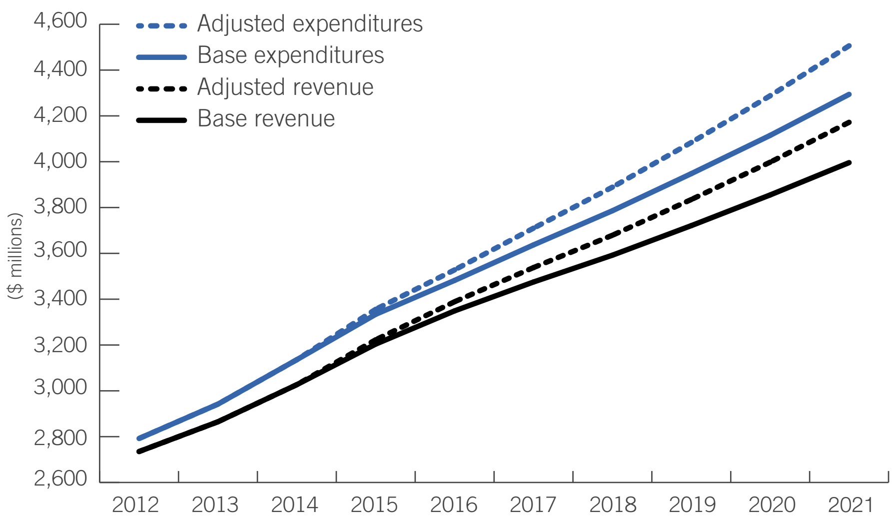
Chart 4
Operating sensitivity analysis – population growth increases annually by an additional 0.5%



Inflation Rates

Forecasted inflation rates were increased by one per cent per year to determine the effects on projections. The operating gap would increase by $30 million to a total of more than $330 million in 2021 (Chart 5).

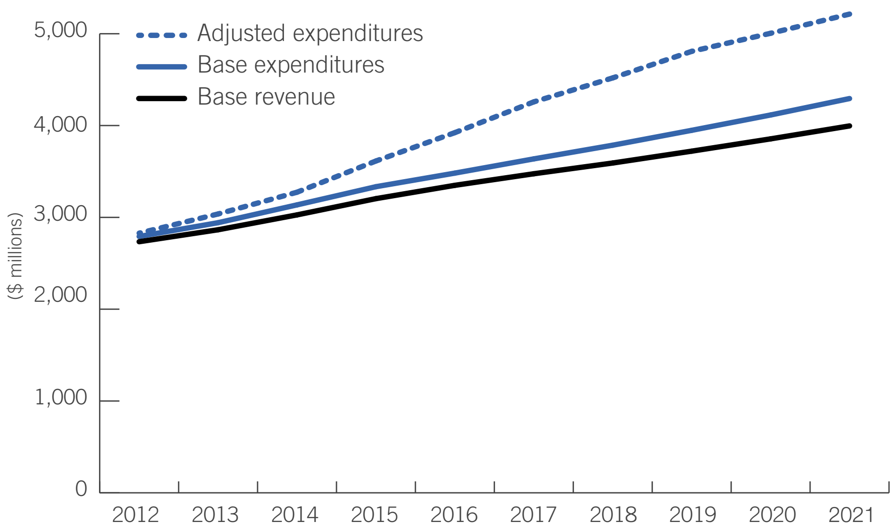
Chart 5
Operating sensitivity analysis – inflation rate increases annually by an additional 1%



Operating Costs of Capital

A sensitivity has been prepared to attempt to quantify the magnitude of incremental operating costs resulting from increased capital expenditures. This scenario assumes that additional non-debt capital funding can be secured and that all current unfunded capital requirements totalling approximately $7 billion can be satisfied. Assuming that the incremental capital is financed using $7 billion in non-interest bearing funding over 10 years, the incremental labour and non-labour operating expenditures would be approximately $900 million as shown in Chart 6. This underscores the importance of fully considering the operating expense impacts of proposed capital projects. This scenario does not consider the additional impact of asset amortization on these incremental capital expenditures.

Chart 6
Operating sensitivity analysis – completing all unfunded capital projects



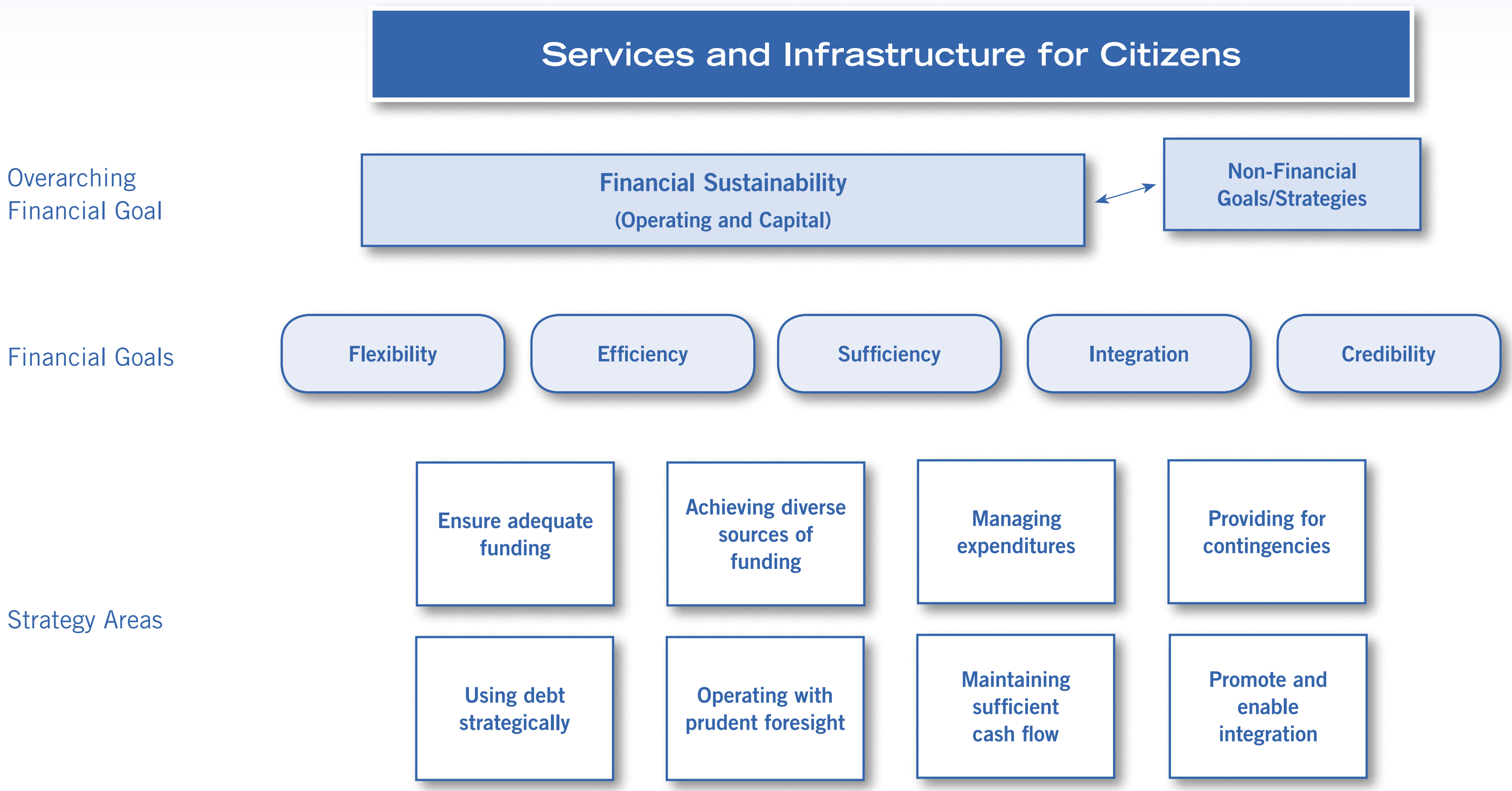
Scenarios

Many variations are possible on the assumptions, so alternative scenarios have been considered to demonstrate the impact of certain strategies being suggested within this document. The outcomes of these scenarios are presented in the "Financial goals and strategies" section of this document in the relevant strategy area. These scenarios are not intended to definitively quantify the anticipated impact of a proposed strategy. They are instead intended to provide insights into the magnitude of change associated with changes to given assumptions. Scenario analysis is a useful tool to help understand the potential risks and benefits of proposed strategies.

4. Financial goals and strategies

The City of Calgary is facing a number of challenges to its capacity to provide the services and infrastructure expected and valued by Calgarians. Systemic barriers such as insufficient and inflexible sources of revenue, unreliable and often conditional long-term capital funding from other orders of government, tax increase resistance, and over-contribution of taxes to other orders of government limit The City's ability to fulfill its municipal mandate to provide services and infrastructure to citizens. Furthermore, growth-related expenditures and growing demand for infrastructure are placing an unrelenting strain on The City's financial capacity.

The essence of the LRFP is to provide a plan to deal with the 10-year financial challenges facing The City, in order to progress toward long-term financial sustainability. The model below presents the conceptual view of how this plan is structured, from the identification of the overall purpose of municipal government, to the specific financial strategy areas that will in turn guide the development of actions through the next rounds of business planning. A connection with non-financial goals and strategies is indicated as well.


Services and Infrastructure for Citizens
Overarching Financial Goal
Financial Sustainability
(Operating and Capital)
Non-Financial Goals/Strategies
Financial Goals
Flexibility
Efficiency
Sufficiency
Integration
Credibility
Strategy Areas
Ensure adequate funding
Achieving diverse sources of funding
Managing expenditures
Providing for contingencies
Using debt strategically
Operating with prudent foresight
Maintaining sufficient cash flow
Promote and enable integration

A brief description of each element of the model follows:

City purpose: The City of Calgary Corporate Mission (Proudly serving a great city) and Vision (Working together to create and sustain a vibrant, healthy, safe and caring community) are expressed through providing services to the citizens of Calgary, including infrastructure and programs that fulfill the responsibilities of a municipal government. Council has recognized that under existing circumstances The City will be challenged to fulfill its municipal mandate. Council has adopted a Plan for 2012 – 2014, the vision of which is to build a municipal government that is more citizen-centred, cost-conscious and innovative. Council's Plan recognizes that existing principles and practices governing municipal finance must change if The City is to continue to provide the services expected and valued by Calgarians without jeopardizing its financial position.

Overarching financial goal: in order to preserve the ability to continue meeting the main civic purpose, The City of Calgary must achieve a sustainable long-term financial situation. The City of Calgary provides over 500 services ranging from social and human services to physical infrastructure. Managing these demands is particularly challenging given a narrow revenue base that, typically, experiences only modest growth. The City is further challenged by a history of economic boom and bust cycles. Periods of strong economic growth typically see demands for a corresponding increase in infrastructure and services, without a corresponding increase in funding and revenue.

In order to define strategies and actions for becoming sustainable, as well as assess the degree to which sustainability is being achieved, a clear understanding of financial sustainability is necessary. For the purpose of this document, financial sustainability is defined as:

> "The enduring ability of The City to ensure that it can deliver the level and types of services expected by the community, while proactively assessing and managing associated risks, at acceptable levels of taxation and fees."

Financial sustainability as defined above extends beyond the ability to raise sufficient revenue to meet the current expenditures. There are four key concepts ingrained in this perspective. The first concept in this statement is that this occurs over the long term and therefore extends beyond the current budget. Financial sustainability therefore means the ability to balance these revenue and expenditure constraints over the long term. Focusing on the long term also implicitly satisfies the need to maintain inter-generational equity, such that one generation does not subsidize the service level to another generation. The second concept is that service levels should be maintained. This puts a constraint on expenditures, in that to be considered sustainable, a municipality cannot continually reduce expenditures to balance with revenues. Third, the importance of The City's proactive risk management culture is acknowledged. Strategies and actions developed and implemented in support of financial sustainability will be fully considered in accordance with a comprehensive set of risk management procedures and programs. Finally, an acceptable level of taxation and user fees means that there is an upward constraint on the ability to raise revenue in order to meet expenditures.

Financial sustainability is not a static goal. Changes in everything from technology to political environment to societal values will all impact the sustainability of The City. Therefore, on-going monitoring and revision of goals and strategies is necessary to ensure that the financial path that The City is on at any given time is sustainable.

Specific financial goals: there are five main goals to deliver financial sustainability in the long term:

- **Flexibility:** being able to effectively respond to changing circumstances, which may relate to economic, social, environmental or political conditions. This goal involves reserving some capacity during typical years to be able to respond to significant atypical conditions or events.
- **Efficiency:** using public funds in ways that provide the highest level of needed services possible within the amount of funding available. Efficiency should be interpreted on two levels: a service level and a corporate level. At the service level, business units need to strive to use the least resources to provide a given level of service. At the corporate level, this means targeting resources at those services most valued by citizens and only providing services that provide sufficient value to citizens to justify the costs.
- **Funding sufficiency:** having sufficient resources to support the delivery of services for which The City of Calgary bears responsibility. As related to financial sustainability, this goal refers not just to the amount of funding, but the consistency in funding level changes relative to changes in expenditures and the diversity of funding sources. The City is continually challenged to fund its significant service obligations because of insufficient and inflexible revenue-raising tools.
- **Integration:** ensuring that the financial constraints under which The City operates are fully considered when engaging in policy-making and decision-making. This also refers to decisions across the Corporation being coordinated to ensure consistency and the most cost-effective service delivery.
- **Credibility:** achieving financial performance in a way that achieves and maintains public confidence in the municipal corporation's ability to provide services and infrastructure at expected levels. This includes the transparency with which financial decisions are made and the accountability for ensuring these decisions are consistent with the overall goal of financial sustainability. Citizens value the services they receive from The City and must continue to perceive that the benefits provided by City services are at least in proportion to the municipal taxes they pay.

Financial strategy areas: eight principal areas of financial strategy have been identified to contribute to the five financial goals over the next 10 years. For the most part, the strategies contribute to all the financial goals identified. Each strategy area is outlined below, including a description and specific statements that support each strategy area. The strategy statements discuss identifiable successes and promote new actions and approaches that will improve financial sustainability, as well as encourage the continuation of current practices that prevent the erosion of sustainability. Included in this section are examples of specific accomplishments toward long-term financial sustainability and proposed near-term and longer-term action items that are being considered or actively pursued by The City in its quest to achieve sustainability.

Council has adopted a Fiscal Plan for The City, the vision of which is to build a municipal government that is more citizen-centred, cost-conscious and innovative. Council's Plan recognizes that existing principles and practices governing municipal finance are not sustainable. The statements contained in the LRFP include strategies and actions that respond to Council's Plan for 2012-2014, which forms the basis for the current cycle of business planning. Actions such as these – and others yet to be identified – would also be included in future cycles of business planning in order to continue to implement the identified strategies and achieve the desired goals.

Strategy areas

1. **Ensuring adequate funding** recognizes the challenges facing The City because of systemic inadequacies that result in insufficient and inflexible revenue-raising tools. It involves both determining The City of Calgary's funding requirements (including managing growth, redevelopment and infrastructure renewal needs, lifecycle replacement and day-to-day operating commitments) and obtaining adequate funding from multiple sources to meet them. It encompasses a balanced approach to capital funding so that needs related to infrastructure growth and maintaining current assets are both prominent. It also requires a thorough understanding of the timing and nature of operating expenditures to ensure that they are matched with stable and reliable funding sources.

   This strategy area includes three major strategy statements regarding full cost identification and maintaining or potentially increasing funding from existing and new revenue sources.

   a. **Ensure that estimates of future service and infrastructure expenditure requirements are complete and sustainable, including all cost elements and the expenditures needed to provide adequate service levels to the existing community and its anticipated growth.**

   In addition to obtaining funding, this strategy requires that the entire cost of providing the required level of service by each business activity is identified in order to establish what level of funding would be considered "adequate". Developing a comprehensive understanding of a service's cost profile over time will ensure that the funding needs are clearly identified, increasing the likelihood that available funding is sufficient and timely. This also implies that the level of service is defined.

   The City has implemented the new financial reporting model required by the Public Sector Accounting Board for municipalities in Canada. A useful outcome of this has been determining the cost of City-owned assets. The Tangible Capital Asset inventory, historical costing and categorization project that was required in order to implement the reporting model has given The City a much-improved understanding of the cost of each asset and what funding will be required to replace it at the end of its lifecycle. As well, linking the long-term operating costs of capital projects has become more rigorous, with such considerations now part of the capital decision-making process.

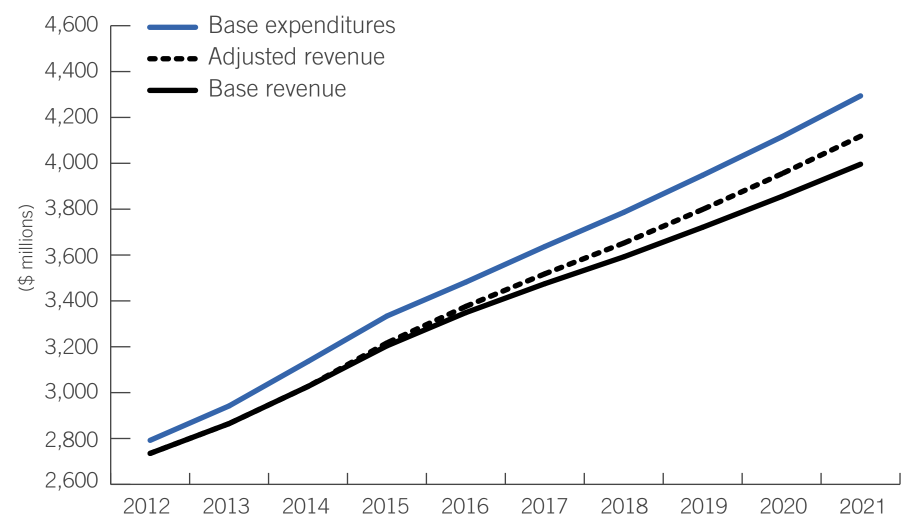
b. Maintain/increase funding from existing sources.

On the funding side, The City has obtained and leveraged Municipal Sustainability Initiative grant funding and made policy changes to increase pay-as-you-go funding for capital projects. Additionally, a review of user fees and subsidies recently undertaken has led to more-accurate costing of services. This revision to the user fee policy can help to better align user fees with the services funded. A recent review of development levies will promote a more representative alignment of these assessments with the costs of providing capital and will provide mechanisms to more accurately align revenues and costs over time. It is also important to remain cognizant of the associated future operating costs of capital and to ensure required operating funds are recognized. Clearly identifying the service impacts of changes to the property tax rate, and the property tax rate impact of service changes will assist in ensuring consistent decisions regarding property tax rates and service levels.

An understanding of the sensitivity of property tax revenue to property tax rate changes can be gained by considering an alternative operating projection. In this scenario a one percent base property tax increase is added each year for the final seven years (2015 – 2021) of the projection period to address the operating budget gap or some of the infrastructure operating maintenance gap.

This scenario demonstrates that the operating gap would be cut by approximately one-third to $175 million in 2021, as a result of the additional one per-cent property tax increase each year, compounding to a cumulative additional increase of more than seven per cent by 2021 as seen in Chart 7.

Chart 7
One per cent per year property tax increase 2015 – 2021



In June 2011, Council approved a comprehensive set of policy and practice changes intended to improve the financial position of the Utilities. In addition, Council also approved higher rates for water and wastewater to better reflect the higher costs associated with providing water and wastewater services to Calgarians. These actions combined will provide the Utilities with improved financial capacity to meet the challenges associated with maintaining service and responding to growth.

c. Match the volatility of revenues and expenditures

Where possible, attaching revenues to operating expenditures that have similar volatility or risk profiles can ensure a long-term stable funding source. For example, explicitly directing franchise fees to utility cost payments ensures that as utility costs rise, the revenue used to fund these costs also rises. This allows The City to more explicitly model and take advantage of natural hedges within City operations.

The types of actions flowing from the execution of this strategy area, in the near-term, include identifying the full cost of service provision (including depreciation), improving the forecasting of service demands and costs, and recognizing lifecycle costs and the operating expense for capital assets, as part of the completion of asset management plans, monitoring and updating user fees and subsidy policies, and reviewing the revenue and expenditure profiles of The City's operations. Longer term, this strategy could encompass, for example, ensuring development agreements provide sufficient resources to fund growth-related infrastructure, and continuing work to achieve certainty, flexibility and longevity in intergovernmental funding agreements.

These types of actions need to ultimately reduce the 10-year projected gap between revenues and expenditures. To date, projected gaps show no significant reductions, emphasizing the continuing need to establish more stable, long-term sources of growth-sensitive funding.

2. **Achieving diverse sources of funding** includes identifying actions related to alternative and innovative funding sources that will help The City respond to the pressures of growth and redevelopment and reduce the reliance on the property tax. This is especially important for large capital requirements such as LRT extensions or water treatment plants. The City has traditionally had access to a limited number of inelastic revenue sources such as property taxes, user fees and intergovernmental transfers to meet expenditure requirements that are continually under upward pressure. This has placed The City's financial position under ongoing stress.

a. Seek alternative and innovative sources of revenue.

The City recently added a levy and fees that have strengthened some existing sources of funding by directly charging the beneficiaries for some services previously funded by municipal taxes. These include the Community Revitalization Levy (that will fund infrastructure upgrades and replacements in The Rivers district) and waste disposal and recycling fees. The addition of the latter two new user fees will change the balance among existing types of funding.

As part of the principles underlying the current development agreement there is direction for The City to work with the development industry to approach the Province for legislative changes that will allow a better funding model for growth infrastructure.

Council recently approved a Fiscal Plan that, among other things proposes changes to the existing rules of municipal finance to ensure better financial capacity. The City of Calgary will advocate aggressively for a new relationship with the Province, including a potential City Charter and the reduction of The City's reliance on the property tax as a funding source. In addition, Council is proposing undertaking renewed initiatives with the Federal government to achieve sustainable, predictable funding for infrastructure needs, with particular emphasis on transit, roads, housing and water infrastructure.

Diversifying funding relates to risk mitigation by having a variety of (and balance among) funding sources that limits the impact to revenues (and therefore services) from economic, environmental and/or social changes and allow for better alignment of changes in revenues and expenditures. Efforts in the short-term could involve establishing a funding mechanism to support the lifecycle maintenance costs for City assets, reviewing rates that apply to City services provided to communities outside the city but within the Calgary region, and identifying additional revenue-sharing or compensation opportunities with other orders of government in order to support both operating and capital needs. As well, the implementation of redevelopment levies in areas beyond the Centre City can offer an alternate source of funding for the upgrades needed in these areas.

Longer-term, The City could focus on identifying and negotiating for municipalities' access to growth-sensitive revenue sources in terms of taxes, fees and development charges; and exploring innovative funding methods used by other governments to meet public needs such as district infrastructure surcharges.

While there have been numerous attempts to add to the sources of operating funding over the years, the percentage of operating revenue coming from property taxes has not changed for many years. The City's own experience with LRT Park and Ride fees and Toronto's recent decision to eliminate a short-lived car registration tax indicate that there are challenges to be overcome, particularly in terms of public resistance. These examples emphasize the need for commitment to support these changes despite initial perceived resistance. Efforts need to continue in this area. The measure of what portion of City operating revenues is provided by municipal property taxes will be a good indicator of whether the search for new sources is succeeding.

3. **Managing expenditures** deals with cost containment in order to limit pressure on revenue requirements, maintain market competitiveness and/or preserve capacity to maintain service levels. This is a particularly important area during economic downturns, when revenues are under stress. Developing a thorough understanding of a service's cost profile over time can help ensure that the funding available to support it is sufficient and timely. This strategy area includes three statements regarding cost control and prioritization among civic services.

a. Increase efficiencies in service delivery.

Council has provided direction to Administration to incorporate a greater emphasis on improvements to municipal service efficiency and effectiveness. In response, Administration has proposed:

- Efficiency and effectiveness goals that are embedded within department business plans and budgets.
- Expanded efficiency performance measures.
- Individual efficiency and effectiveness performance goals for General Managers and Directors.
- Regular ongoing service reviews within departments.

In response to this direction, Administration has proposed a strategy for ongoing improvements to service efficiency and effectiveness including a "zero based" review (ZBR) approach. A zero based review is an examination of all aspects of an existing service including scope, service level, alignment with long-term policy goals and potential efficiencies in the way services are delivered.

The strategy proposes a phased implementation of ZBRs, examining one to three business units each year, following a pilot. This approach balances the need for review with cost, organizational capacity and citizens' ongoing expectations for quality services. The findings of these reviews, and the recommendations concerning how these findings should be incorporated into business plans and budgets, have the potential to impact operating projections. These results will be incorporated into future projections as appropriate. The results of a scenario have been included later in this section which considers the impact of a one per cent annual increase in the efficiency with which services are delivered to Calgarians.

Under the Asset Management Policy, approved by Administration in 2010, asset management plans are developed in many business units and will lead to lifecycle management of assets that will target expenditures to achieve efficient life spans while reducing the impact of premature major overhauls or replacements.

Consistent with the principles articulated in The City's Municipal Development Plan and Calgary Transportation Plan, increased residential density and job growth will focus on nodes and corridors served with a high level of transit service. A regional context study for South Shaganappi communities, for example, will help to implement this direction by setting priorities for action, resulting in improved alignment of planning, infrastructure investment and expenditures. Multi-community planning for redevelopment in established areas will also assist in delivering more efficient infrastructure in these areas.

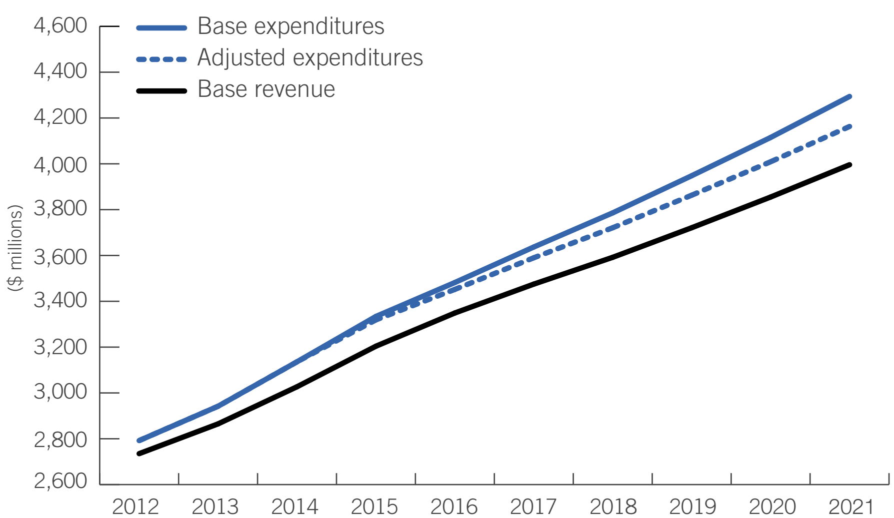
In the near-term, The City will continue to emphasize improved productivity through individual process improvements, better technology, lower-cost alternatives and reconsideration of how services are provided. A few of the many actions that will flow from this strategy include:

- Collaborating with community partners on service provision.
- Ensuring there is alignment among Council priorities, coordinated department business plans and corporate budgets.
- Implementing innovative procurement and inventory management strategies.
- Incorporating sustainable strategies into facility design and construction.
- Improving fuel management practices and using LEED building standards to reduce energy consumption.
- Increasing the number of online citizen services.

The City will also carry out a benchmarking program with comparable municipal governments to establish the degree of economy and effectiveness in City of Calgary services.

Given that a significant portion of The City's operating budget comprises labour and associated costs, gains in productivity and efficiency have the potential to yield significant savings. Chart 8 illustrates the sensitivity of the operating gap to an increase in efficiency. In this model, a one per cent annual efficiency increase between 2015 and 2021 yields potential operating cost savings of approximately $130 million over 10 years, all other factors being equal.

Chart 8
Operating sensitivity analysis – labour efficiency increases one per cent per year from 2015 – 2021



b. Set spending priorities to ensure the most important areas are funded.

The City has put in place various business unit and corporate capital prioritization business processes to optimize the overall capital expenditure and provide guidance for potential cost deferrals in the future. Measurement tools have also been identified and developed to assist with managing assets, including the facility condition index and pavement quality index.

Planning processes have also focused additional attention on managing expenditures. In its update of the Municipal Development Plan, the Plan It Calgary project emphasized that financial sustainability needs to be included in planning for growth. Long-range capital expenditures are being coordinated and mapped by quadrant, which could lead to more complete communities rather than planning too many communities and spreading resources too thinly around the city. City results are being compared to benchmarks used by other municipalities in Canada.

As part of The City's evolving budget process, a service identification review is being implemented. This will consider options related to how budget information can be presented to make it more meaningful to stakeholders. Providing a more functional identification of services and infrastructure will assist in enhancing visibility and promoting understanding of services important to citizens. Council also approved the public engagement process for the combined Core Services review and the business planning and budget coordination process. This is a three-phase public engagement process that will gather information from citizens, employees and Council about the most valued City services and priorities and how budget dollars should be allocated to provide desired services now and in the future.

Longer term, The City could pursue options involving evaluating the standards that determine the level of civic services provided; aligning economic and population growth with infrastructure investment planning, land use planning and operating and capital budgeting; and assessing the scope and delivery approach for City services.

c. **Position Calgary as an efficient provider of similar services and infrastructure relative to other comparable municipalities.**

This strategy area relates to the specific challenge of allocating scarce resources among many competing public demands. Expenditure management is an on-going requirement of all organizations. City business units continually seek ways to limit expenditures and improve efficiency. The cost of municipal government per household can provide a measure of how successfully expenditures are being managed when adjusted for inflation and the level of scope of services being provided. There has been a good deal of success in managing expenditures. At the same time, it is a strategic area that will always benefit from further review and action, as well as continued benchmarking.

4. **Providing for contingencies** prepares The City to manage risk and to be resilient when dealing with unforeseen circumstances while limiting the impact on services, as emphasized by the worldwide economic upheaval of the recent past. The following two strategic statements address the means to prepare adequately for the unknown.

a. **Monitor economic and operational factors and forecasts in order to be able to respond to changing circumstances.**

The economic downturn and variable funding schedules from other orders of government (for example, MSI and Green Trip funding) has highlighted the need to monitor the external economy and internal expenditures to be aware of the timing and degree of contingency actions and funding that may be required. The City is evolving a budget process that provides mechanisms to adjust business plans and budgets to correspond to changes in funding levels. In addition, The City maintains and monitors key operational and economic indicators that have the potential to affect corporate performance.

The City has also implemented measures to manage operating budget volatility. Natural gas costs, diesel fuel and US dollar transactions are hedged to manage exposure to price fluctuations and provide more certainty and stability in managing expenditures. In addition, The City entered into a twenty year contract with its electricity supplier to mitigate volatility associated with this utility cost.

Further actions which The City could pursue in the short-term include: preparing impact assessments for City services based on a series of economic scenarios; developing actions to correspond to identified risk levels; moving toward target levels for unallocated reserves, and reviewing policies regarding the allocation of additional revenues that exceed budgeted amounts.

b. Ensure The City has ready access to enough funds to meet unforeseen urgent needs and manage risk appropriately.

The City of Calgary has focussed significant attention on contingencies in recent years. 10 per cent of Municipal Sustainability Initiative funds were set aside for contingencies, some of which has been allocated for debt servicing; cost escalation contingencies were added to capital projects; and the Fiscal Sustainability Reserve (FSR) minimum and target levels were increased along with the approval of new potential funding sources. The FSR balance was increased to almost $225 million, which is a good start to moving towards the target of setting aside 15% of gross annual expenditures for emergency purposes.

Good progress has been made in this area. A continuation of the trend will confirm the strategy is achieving the required results.

5. **Using Debt Strategically** can provide capital funding flexibility by allowing certain infrastructure to be built and used before sufficient revenue has accumulated to offset the needed investment. Debt is also a tool that allows capital investments to be made when construction costs are favourable, and to meet other needs such as stimulating the local economy. Debt can also promote inter-generational equity in that infrastructure is paid for by those who use it. The prudent use of available debt capacity can aid financial flexibility as a source of contingency financing. High debt levels, however, reduce flexibility, can increase the cost of borrowing and could impair financial sustainability if debt repayments cause or contribute to future revenue inadequacy. Two strategy statements deal with ways to improve The City's use of debt.

a. Manage the level of debt and use it strategically to make available, in a timely manner, essential assets with long lifespans.

In 2008, Council approved recommendations that limit The City's overall debt. While approving up to $100 million annually in self-sufficient tax-supported debt from 2009 to 2013, no other new tax-supported debt capacity was approved. Ongoing principal repayments reduce existing debt, but self-supported utility debt has been increasing in recent years due to the need for major capital infrastructure projects. This has exceeded increases in total debt capacity created by growth. A financial policy review has been conducted to assess the validity of existing policies and add others where necessary in order to ensure that the policies in place will serve to maintain financial viability and sustainability of the Utilities as a fully self-supporting entity. The City can also set an internal limit relative to the MGA debt limits to ensure that sufficient debt capacity is available during recessionary periods or during other atypical events.

The City will be temporarily extending its use of debt for strategic purposes. The status of credit ratings and debt ratios that are used by the Alberta Government and The City can then be used to track progress on improving the measures to strengthen contingency capacity. Examination of other debt financing options will increase flexibility in how debt can be used for civic purposes.

b. Examine a wider range of debt financing instruments

Strategic use of debt for bridge financing for MSI-funded projects has been approved to get an earlier start on projects funded through provincial grants. Short-to medium-term debt will temporarily increase, but this type of debt would be considered self-sufficient because some future provincial funding would be dedicated to repaying it. This strategy has allowed The City to successfully maintain momentum behind projects despite changes to the sequencing of funding commitments.

For capital financing, Council's policy on considering private-public-partnerships (P3s) may contribute to diversifying sources of financing by enabling The City to take advantage of potential private financing sources and spread costs over the useful life of the asset while transferring long-term risk to a private partner. As well, in some cases, access to grants from other orders of government may be contingent on the project considering a P3 as a delivery method.

The City is currently pursuing a P3 model for the development of a bundle of four new recreation facilities in Calgary. This model will involve a private partner that will be responsible for the construction of all four facilities, building operations and maintenance, and lifecycle costs. A programming partner will be responsible for the recreation, sport and cultural programming offered at the facilities.

This arrangement provides four key benefits to Calgarians. First, the four bundled facilities are estimated to cost less in the long run under the P3 model than under a traditionally financed and operated model. Second, the recreation centres will be available for the use and enjoyment of citizens more quickly than under a traditional model. Third, the facilities will be delivered under a fixed-price, long-term contract that provides budget certainty and ensures timely completion and maintenance of the facilities. Finally, the programming partner(s) will be contracted separately and will accept some risk associated with revenue and will also be responsive to the program needs of the community.

In the near-term, The City is examining such options as continually monitoring debt levels and credit ratings, and timing capital investments in relation to economic cycles. The City is also looking at ways to better manage debt associated with growth through the sharing of risk between The City, developers and builders.

Longer-term, The City may examine options that involve:

- Expanding the sources of debt financing beyond the current arrangements through the Alberta Capital Financing Authority (for example, private placement bonds, municipal bonds or pension fund investments).
- Better matching of types of debt financing with the type of capital infrastructure (e.g. revenue bonds for revenue-generating capital works and, more Tax Increment Financed projects and developments).

6. **Operating with prudent foresight** requires The City to take into account what the current and future impacts of decisions will be on services and infrastructure, including how The City's overall financial sustainability may be affected. The two strategic statements included here are largely related to maintaining and extending existing practices regarding a longer-term approach to decision-making.

a. Ensure the services The City provides are well defined and are linked to dedicated financial resources required to provide them.

There have been improvements to consistency in the capital budget process that formulate and prioritize infrastructure investment plans (IIPs). Efforts are being made to ensure operating budget impacts are included when capital projects are approved. The Directors' Integrated Growth Committee will provide recommendations to the General Managers' Strategic Growth Committee regarding where the City will facilitate and invest in growth and change through redevelopment and expansion of the urban form. Commencing new local area plans will require amendments to the Municipal Development Plan, which is a decision of Council following a public hearing.

Planning processes provide long-term views of City finances, infrastructure, services and development. Maintaining and building on existing processes will ensure that future possibilities are identified, evaluated and acted on.

b. Build internal and external awareness of the projected future costs of City services and infrastructure and of the potential impacts of changes to those projections.

A number of processes have been identified to help clarify and guide future actions to improve financial sustainability. There is an explicit policy in The City's Municipal Development Plan to ensure municipal financial sustainability is considered within its growth-management strategy. The City has extended its financial planning horizon with three-year business planning and budgeting as well as the 10-year period for long-range financial planning.

The City is committed to promoting a deeper understanding with Council, administration, Calgary's citizens and other orders of government about this organization's financial realities and to create additional support for City initiatives to move toward financial sustainability. The City recently introduced a new process of engagement related to the budget process to test the alignment between citizens' and The City's priorities. Stakeholders, including citizens, City employees, community organizations and associations were invited and encouraged to identify and confirm immediate priorities while keeping an eye on the longer term vision that will support the future that Calgarians envision. Over 23,000 citizens, employees and organization participated in conversations about City services, values and priorities. The results of this process indicate that stakeholders appreciated being asked for their opinions and they also value the many programs and services The City offers.

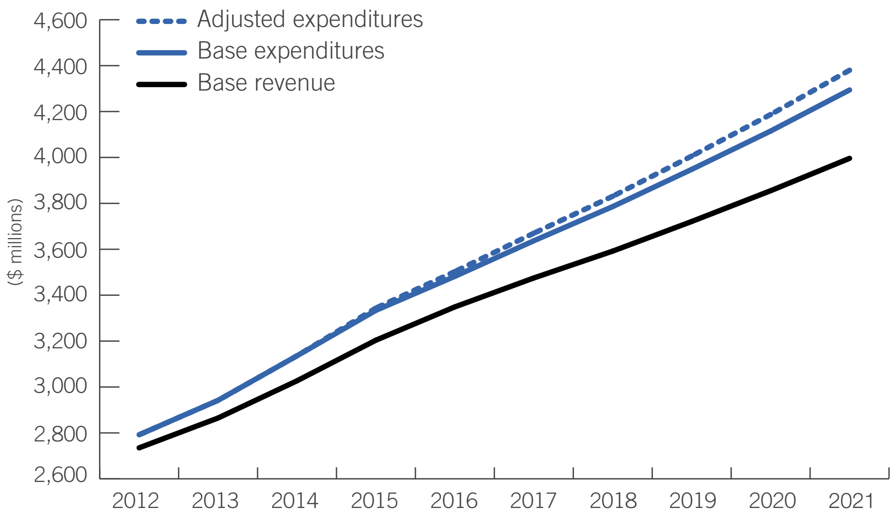
In the short-term, The City will pursue a wide range of actions related to this strategy area, emphasizing:

- Continuing to integrate business plans and budgets.
- Assessing the longer-term impacts of current financial decisions (such as providing for the operating impact of capital investments).
- Incorporating considerations of financial capacity into The City's decision-making on growth and land use planning.
- Improving financial projection models to provide scenarios related to economic uncertainty.

To assist in understanding the longer-term impacts of current financial decisions a scenario has been prepared which considers gradual increases to operating spending to begin to close the operating infrastructure gap identified in the 2010 ISR. This was done by adding an additional $10 million in expenditures in 2015 and increasing by a further $10 million per year until 2021, when the additional annual spending levels off at $85 million which is the estimated annual shortfall in operating maintenance spending.

This would result in the operating gap rising to approximately $390 million by 2021 (compared to $300 million in the base model). This level of spending would still fall approximately $470 million short of eliminating the estimated $860 million 10 year operating maintenance gap identified up to 2020 in the ISR. Chart 9 illustrates the magnitude of this change.

Chart 9
Operating sensitivity analysis – operating expense increases by $10 million per year from 2015 – 2021 to fund ISR operating gap



7. **Maintaining sufficient cash flow** allows The City to pay the costs of supplying services and infrastructure mandated by Council while managing the use of debt. The single strategy statement refers to the need to spread cash flow throughout the year to reasonably match expenditure requirements.

a. **Ensure The City receives sufficient cash flow spread over the year to meet obligations while minimizing debt requirements.**

The City's long-standing promotion of its monthly payment plans for business and property taxes ensures that the majority of its revenues are spread throughout the year, reducing the volatility of cash flow and requirements for short-term borrowing. The participation rate for the TIPP program for property taxes has stood at just over 50 percent for a number of years.

The City's cash flow meets its requirements. Periodically measuring the level of participation in the monthly tax payment plans will provide a yardstick for adequately maintaining it.

Actions that respond to this strategy statement could include looking for opportunities to advance revenue intake, continuing support for instalment payment plans for City taxes, and pacing expenditures to maximize cash flow. For example, The City could potentially make the monthly payment plan mandatory for all taxpayers.

The City could also enhance processes to ensure that estimates of expenditures reasonably consider the amount and timing of outlays. For example, capital budget requests should be reasonably estimated to match the anticipated spending timeframe based on a realistic construction schedule. This would assist in reducing significant capital budget carry-forward amounts.

8. **Promoting and enabling integration** of priorities and resources involves identifying and encouraging awareness of the financial implications of policy-making and decision-making on The City's financial position. It involves three strategy statements regarding the optimal delivery of services and infrastructure.

   a. **Align corporate priorities among Business Units and stakeholders by linking needs and actions to resources, responsibilities and timelines.**

The most significant initiative currently underway to promote and enable integration is The City's 2020 Sustainability Direction. This is a 10 year strategic guide for transformation within the context of longer-term plans and strategies. It identifies 10 year goals and objectives with clear measures of success as well as high level, integrated strategies with priority leverage areas. It provides all departments with a consolidated direction for community well-being, a prosperous economy, sustainable environment and smart growth and mobility. The 2020 Sustainability Direction is the road map that identifies where the organization would like to be in 10 years and, at a high level, how it is going to get there, just as business planning is the process that identifies where the organization is, where it would like to be in three years and how it is going to get there. An efficient and effective corporation possessing adequate and enduring financial capacity is identified as being critical to achieving sustainability. In October 2010, the Administrative Leadership Team approved the 10 year goals and objectives supporting this initiative.

In 2010, Administration approved an Asset Management Policy to govern the practice of asset management within The City. The policy identifies specific principles to ensure that The City's approach to asset management is, among other things, "holistic, systemic, sustainable, integrated and aligned". The policy also clearly identifies the risk associated with conflicting business unit investment priorities, issues with the coordination of delivery of service, corporate inefficiencies, and lack of expenditure optimization.

The Tangible Capital Assets (TCA) program will have impacts across the Corporation. The mission of the project is to embed sustainable TCA processes throughout the organization by improving integration with Asset Management. The intent is to create an integrated approach to managing, recording and accounting for The City's Tangible Capital Assets by promoting procedural enhancements that strengthen business processes, increase operational efficiency and facilitate more comprehensive decision-making.

The Asset Management Policy and the Tangible Capital Asset program have provided The City with a much-improved understanding of the lifecycle costs of its assets. Longer-term, The City could pursue initiatives that would allow it to leverage this information into a multi-faceted decision-making model to support optimal planning for the growth, maintenance and replacement of existing assets and the development of new assets.

b. Increase co-ordination to promote greater efficiency by reducing duplication of effort or working at cross purposes among different Business Units and stakeholders.

There is an explicit principle in The City's Municipal Development Plan that supports a strategic framework for growth and change. This framework will ensure that policy, strategy and resources for growth are better aligned to facilitate Calgary's supply of planned and serviced lands and incorporate the implications of capital and operating expenditures into growth decisions.

The process of defining a growth management framework for The City is on-going and dynamic. In the near-term, the organization will actively pursue opportunities to develop more objective and cross-Corporate processes to identify growth priorities and directly link the identification of planning needs with supporting infrastructure and service delivery. In addition, The City will:

- Seek to make land use planning and investment decisions within a strategic, inter-departmental process.
- Coordinate infrastructure investment priority lists and identify opportunities to prioritize capital project spending and to accommodate and manage growth, consistent with principles and objectives contained in The City's Municipal Development Plan and Calgary Transportation Plan. One of the key processes to be developed requires full incorporation of capital and operating expenditures into growth decisions, including Regional Context Studies and Local Area Plans.

c. Develop corporate prioritization processes for growth in existing brownfield areas and new green field areas.

The City has recently proposed a framework that will provide the principles and plan necessary to facilitate the more effective management of growth and the financial challenges it presents. Urban growth and development entail very real financial commitments of operating, capital and lifecycle costs. The City must be fiscally responsible and ensure that growth and change occur within its financial capacity.

The proposed framework for growth and change includes, among other elements, a logical and strategic approach to development which recognizes the need to set and plan investment priorities, and to establish a logical sequence for these priorities in both developing and developed communities to realize the objectives of the Municipal Development Plan and the Calgary Transportation Plan. Prioritized growth must recognize The City's strategic interests, the logical, efficient and economical provision of services, the ability to accommodate change over time, and both community and landowner interests.

5. Summary and conclusions

Summary

The current financial situation of The City of Calgary reflects a strong financial position, prudent fiscal practices, low residential tax rates, solid reserves, high but manageable debt and an AA+ credit rating. Although The City's financial position is sound there are some systemic and emerging issues that could potentially threaten The City's financial sustainability. Without action to address these issues, The City will become increasingly challenged to provide the services and infrastructure that citizens expect and value.

The Long Range Financial Plan provides a view of the gap that could arise between The City's revenues/funding and expenditures in the next 10 years if these systemic and emerging issues continue unaddressed. The LRFP also provides financial goals, strategies and actions to reduce the gap and improve The City's financial sustainability.

The LRFP provides 10-year projections, examples of planning projects that could have significant financial impacts, and financial goals and strategies in one forward-looking document. The LRFP is not an exercise in precision, but remains a work in progress which lays the groundwork for improvement with each update.

The 10-year operating and capital projections in the LRFP have been calculated based on assumptions that would maintain only existing types and resourcing of service and infrastructure.

The operating revenue and expenditure projection for the 10-year period 2012-2021 results in increasing annual operating shortfalls of approximately $300 million in 2021. Addressing the infrastructure maintenance deficit could increase that shortfall significantly.

The capital funding and expenditure projection for the same period shows annual shortfalls of more than $700 million through 2021 and totalling approximately $7.0 billion for 2012-2021.

Financial goals and strategies have been developed and need to be periodically reviewed to improve financial sustainability while considering areas that need to be maintained to prevent City finances from deteriorating.

Conclusions

Council has identified that existing principles and practices governing municipal finance are unsustainable and must change if Calgary is to maintain and enhance its current financial position.

Over the next ten years, the City of Calgary will require approximately an additional $7.0 billion in revenue and funding to meet the current level of citizens' expectations for services and infrastructure. Current sources and levels of revenue and funding are not sufficient to meet projected requirements. The City will also be further challenged by continued growth, economic volatility and tax resistance.

Without action to address these challenges, The City will face increasing financial pressure in providing services and infrastructure that Calgarians expect and value. The potential funding gaps identified in this document indicate that continuing to provide the same services in the same way with the same revenue and funding is not financially sustainable. Ensuring that the right services are delivered as efficiently and effectively as possible will provide some relief to the financial pressure facing The City. However, The City also needs to develop and implement actions that support necessary financial strategies identified in this document in order to achieve those financial goals that will maintain or enhance financial sustainability, while continuing to provide services and infrastructure expected and valued by Calgarians.

Progress has been made on implementing strategies identified in previous LRFPs and this momentum needs to continue. The impacts on The City's financial projections will need to be monitored to determine effectiveness and whether strategies or implementations need to be adjusted. Administration will periodically update the LRFP to reflect Council decisions, changes to the economy and internal and external developments that affect The City financially.

6. Appendices

Appendix 1

Process of developing the LRFP

Developing Calgary's first LRFP was a lengthy and challenging process. After some early work in 2004 to lay the foundation and get Council's approval for the concept of developing a long-range plan, work began in earnest in 2006 following Council's approval of a multi-year business planning and budgeting approach. The work proceeded in three main phases:

- Learning about other cities' approaches to long-range financial planning.
- Developing assumptions (the updated list is in Appendix 2) and building the 10-year operating and capital projection model, in concert with the development of a three-year operating budget projection model, to improve the tools to do longer-range projections.
- Creating draft financial goals and strategies based on the projection results and the financial policy work already done in several areas such as capital financing, reserves and multi-year budgeting.

The LRFP project was managed within the Corporate Financial Planning, Budget and Reporting section of the Chief Financial Officer's Department, but involved staff at many levels throughout the organization, including the Administrative Leadership Team (ALT), the Senior Management Team (SMT), the Finance & Supply management team and the project managers from several related corporate planning projects. There were a number of focus groups to gather information on the assumptions to use in the financial modeling, on the financial goals and strategies to respond to the 10-year projections, and on the means to evaluate progress being made toward improved financial sustainability.

The City of Calgary entered into a longer-term approach to planning and budgeting knowing that its volatile economy made it less than an ideal candidate for building reliable long-term forecasts. In 2006 Calgary experienced the largest single-year population growth in its history, as well as substantially increased local inflation fuelled by higher housing and energy costs. In 2008 and 2009, the global economic recession affected The City's revenue stream substantially. Taking a 10- year view of financial prospects only magnifies the difficulty of making reasonable projections within an environment rife with challenges.

This third LRFP update has involved:

- Consulting with business unit and corporate stakeholders.
- Reviewing and updating assumptions.
- Updating demographic and economic forecasts.
- Obtaining current operating and capital data.
- Fine tuning formulas and calculating projections.
- Reviewing and updating goals and strategies, including reflection of the new approach of the 2012 – 2014 business plan and budget coordination program.
- Reviewing significant accomplishments and establishing measures of progress toward long-term financial sustainability.

Future LRFPs

The LRFP is reviewed on an ongoing basis and is published in an updated form when there is an upcoming need for its projections and strategies. The product will continue to become more useful as our knowledge of long-term trends improves. This LRFP update is based on the 2012-2014 business plan and budget data, and provides background in preparation for Council's consideration of proposed operating and capital budgets and business plans for 2012 to 2014. The LRFP will continually evolve to both reflect and guide stewardship of The City's financial situation.

Appendix 2

Assumptions

ISSUE	ASSUMPTION
Base: operating budget	• Indicative 2012-14 operating budgets. • Includes transfers to the Calgary Public Library (CPL) and from the Calgary Parking Authority (CPA), but not the full operating budgets of CPL, CPA and Calgary Housing Company (CHC).
Base: capital budget	• Preliminary 2012-21 capital budget. • Forecast construction cost increases are already included in the capital budget, capital plan and not funded projects. • 50 per cent of (2012 capital budget + carry forward from 2011) is carried forward to 2013. • Includes CPL, CPA and CHC capital.
Base: capital plan plus not-funded projects beyond the first year	• Capital budget plan and not funded projects for 2012-2021 are included in the base projection. • For each year from 2012-2021, the previous year's carry forward is added to the total cost of planned plus not funded for that year, then 50 percent is projected to be completed while 50 per cent is carried forward. • All unallocated pay-as-you-go and development levies and assessments are allocated to the group of not-funded projects when those funds are projected to become available.
Expected term of specific government grant programs	
• Alberta Municipal Infrastructure Program (AMIP) (provincial)	• As of March 31, 2010 all AMIP funding ended, however, expenses can still be submitted to the program for reimbursement until March 31, 2015.
• Fuel tax sharing (provincial)	• Funding continues at the current level of five cents per litre. • Fuel consumption increases at the same rate as population increase.
• Gasoline tax transfer	• Funding is as specified in the current agreement, then continuing at the level reached in federal fiscal 2009 – 2010 ($59.4 million per year) for the balance of the projection.
• Policing grant (provincial)	• Funding continues at the rate of $16 per capita (total increasing with population)
• Municipal Sustainability Initiative	• Funding included to 2017.

Issue	Assumption
Levels of resources	• Projections based on indicative 2014 expenditure levels to establish baseline. • Unit costs also increase due to inflation.
Levels of productivity improvement	• Assumed to be reinvested to mitigate service level deterioration resulting from increasing complexity of Calgary, including travel distances and congestion.
Impact of population growth on operating expenditures	• Expenditures increase based on population growth factor. • Growth impacts expenditures such as debt servicing and depreciation only through increased borrowing and increased utility assets.
Impact of population growth on operating revenues	• Revenues will increase at 90% of the population growth rate except where individual circumstances apply (e.g. service area and/or infrastructure limitations or additions).
Debt financing	• Additional debt financing capacity is available only for utilities and self-sufficient tax-supported projects after 2007.
User fee rate changes	• Individual fees increase at the same rate as the Calgary CPI forecast. • Results of Fair Calgary and User Fees and Subsidies Review will be incorporated in future LRFP updates.
New services	• No new services are included.
Population growth forecast (affects operating and capital expenditures)	• 10-year projection obtained through City of Calgary Corporate Economics group based on the 2011 civic census results.
Inflation rate forecasts • Salary and wage (55 per cent of operating expenditure) • Non-salary and wage	• Salaries and wages are projected to increase based on Calgary CPI. • Benefits are projected to increase by an average of about 0.6% per year beyond the increases associated with wage and salary rates and staffing additions. • Corporate Economics provided 10-year CPI, commodity (including oil, natural gas and electricity) and other forecasts.
Operating impact of capital	• Incorporated in the impact of population growth on operating expenditures.

Issue	Assumption
Property tax	• Growth will be based on population forecasts. • Rate changes calculated using The City of Calgary municipal price index, which reflects the projected inflationary increases in The City's operating expenditures.
Other revenues	Allocations between operating and capital uses reflect current policies.
• Local access fees (franchise and MCAF)	• Local access fees projections are based on natural gas and electricity price and volume forecasts.
• Business tax	• Growth is based on population forecasts. • Projections do not include any rate increases.
• Fines and penalties	• Growth is based on population forecasts. • Increases for population growth only, except for Police, where no growth is included.
• Dividends and return on equity	• Current policies concerning amounts and use continue. • ENMAX dividend based on $47.3 million annually contributed to the operating budget after 2015.
• Community Recreation Levy, Redevelopment Levy and Acreage Assessments	• The levies and assessments continue to provide funding at their 2014 levels.
Annexation activity	• No annexation is projected from 2015 to 2021, but if one is decided on, it would be added in a future LRFP update.
Capital financing	• Incorporates existing Council decisions. No new changes to policy.

Issue	Assumption
Amortization (depreciation)	• Applied to utilities and self-supported, but not to tax-supported assets until new Public Sector Accounting Board (Canadian Institute of Chartered Accountants) rule impacts can be incorporated into a future LRFP update.
Not specifically included in the base case (included to the extent that they are part of current plans and budgets)	• Financial impacts of planning and policy projects involving Council decisions in the near to medium term: • imagineCALGARY • Plan It Calgary – Municipal Development Plan – Calgary Transportation Plan • Asset Management Plan • User Fees and Subsidies • Fair Calgary • Centre City Plan Implementation • Surplus School Reserve Sites • Regional partnerships • Existing and new capital projects that may be brought to Council for approval of additional financial impacts not included in the 2012-2014 Capital Budget, 10-year capital plan or not funded project list in the capital budget system.

Appendix 3

Total City operating projections ($ millions)

	Budget 2012	Budget 2013	Budget 2014	Projected 2018	Projected 2021
EXPENDITURES					
Wages/Salaries/Benefits	1,547	1,640	1,753	2,140	2,500
Materials/Equipment/Utilities/Services	875	919	973	1,160	1,320
Debt Servicing and Depreciation (Note 1)	297	306	300	330	350
Net Transfer to Reserves	176	183	201	250	270
Transfer Payments	204	215	227	270	310
Net Income Distribution – Utilities	79	87	116	170	160
Recoveries	(387)	(409)	(434)	(530)	(610)
GROSS EXPENDITURES (NET OF RECOVERIES / NET INCOME)	2,792	2,942	3,136	3,790	4,300
REVENUES					
Tax Revenue (Note 2)	(1,326)	(1,396)	(1,474)	(1,790)	(2,040)
Sales of Goods & Services	(886)	(937)	(1,009)	(1,210)	(1,330)
Revenues from Utilities/Subsidiaries	(303)	(306)	(311)	(300)	(310)
Other Revenue	(220)	(226)	(233)	(290)	(320)
TOTAL REVENUE	(2,735)	(2,865)	(3,027)	(3,590)	(4,000)
NET DEFICIT / (SURPLUS)	**57**	**77**	**108**	**200**	**300**

Note 1: includes principal and interest payments for tax-supported as well as interest payments and depreciation for utilities and other self-supported entities.

Note 2: tax increases for 2012 & beyond reflect rate increases at municipal price index and growth matching increases in population.

Note 3: totals may not add due to rounding

Appendix 4

Total City capital projections ($ millions)

	Indicative Budget 2012	2013	2014	Projected Capital Expenditures (including deferrals/carry forward impacts) 2012-16	2017-21	2012-21
EXPENDITURES						
Maintenance	255	266	266	1,230	790	2,020
Upgrade	272	261	233	1,220	960	2,180
Growth	811	737	614	2,970	940	3,910
New Services	74	87	77	460	380	840
Not Funded	139	296	314	2,420	4,230	6,650
TOTAL EXPENDITURES	**1,550**	**1,647**	**1,505**	**8,300**	**7,300**	**15,600**
FUNDING						
Capital Deposits (including MSI)	830	695	548	2,750	710	3,460
Debt	215	285	296	1,470	1,800	3,270
Reserves	366	371	347	1,670	550	2,220
TOTAL FUNDING	**1,411**	**1,350**	**1,191**	**5,890**	**3,060**	**8,950**
FUNDING SHORTFALL	**139**	**296**	**314**	**2,410**	**4,240**	**6,650**

Note: Totals may not add due to rounding.

Appendix 5

Total City statement of financial position projections ($ millions)

	2011	2017	2021
FINANCIAL ASSETS			
Cash, cash equivalents & investments	2,360	1,630	2,640
Other long-term assets	2,260	2,420	2,540
TOTAL FINANCIAL ASSETS	**4,620**	**4,050**	**5,180**
LIABILITIES			
Other working capital	410	410	410
Working capital shortfall	240	3,980	7,170
Capital deposits	830	150	40
Other long-term liabilities	350	350	350
Long-term debt	2,900	3,270	3,550
TOTAL LIABILITIES	**4,730**	**8,160**	**11,520**
PHYSICAL ASSETS	**12,250**	**21,700**	**26,540**
NET ASSETS	**12,140**	**17,590**	**20,200**
NET MUNICIPAL POSITION	**12,140**	**17,590**	**20,200**

Note: Totals may not add due to rounding.

Net financial assets (assets less liabilities) and total non-financial assets (physical assets) comprise The City's "accumulated surplus" which is a net measure of everything owned and owed by The City. The LRFP operating and capital projections contain a gap resulting from revenues/funding sources being less than expenditures. A standard Statement of Financial Position (SFP) based on these projections would not be balanced without having negative working capital values and/or negative equity to compensate for the deficiency created by the operating and capital gaps. To balance the SFP, a line has been added (working capital shortfall) to represent the gap at each year end. This allows the SFP to have normal levels of cash and other working capital rather than depleting them entirely and showing negative balances. This working capital shortfall reflects the cumulative need for additional funding that result from the excess of expenditures over revenues.

While the SFP projection is not fully realistic because of the funding shortfalls, it is a tool to measure the financial impact of changes to assumptions. While the operating and capital projections provide information on an annual basis, the SFP provides a cumulative view over 10 years. Also, the SFP is useful to include because numerous financial strategies relate directly to the SFP. It provides a context when considering the financial goals and strategies.

These statements exclude Calgary Public Library, Calgary Parking Authority, Calgary Municipal Land Corporation and Calgary Housing Company (which are included in The City's consolidated financial statements) as well as other civic partners that are not part of The City's annual statements, and include only the net asset value of ENMAX.

Appendix 6 – Similarities and differences between Strategic Growth and Capital Investment, Infrastructure Status Report and Long Range Financial Plan

Items included in report		Name of Report to Council		
		SGCI	ISR	LRFP
10-year projections	10-year funded amount for infrastructure assets		✓	✓
	10-year unfunded amount for infrastructure assets		✓	✓
	Capital growth of infrastructure assets (funded and unfunded)	✓	✓	✓
	Capital maintenance projections for infrastructure assets		✓	✓
	Operating maintenance projections for infrastructure assets		✓	✓(current maintenance level)
	Condition and age, current replacement value, criticality, at risk asset value		✓	
	Annual capital expenditures based on estimated carry forwards (50 per cent deferred each year of plan)			✓
	Operating projections for non-infrastructure services			✓
	Statement of financial position including all financial and infrastructure assets			✓
Financial goals and strategies				✓
Mapping capital growth projects		✓		
Accomplishments toward financial sustainability				✓
Growth, maintenance, upgrades, service summary by business unit		✓	✓	
Five, 10 and 15-year population projections		✓		
Operational framework for The City's growth management processes		✓		
Market share residential growth trends by planning sector		✓		

Items included in report	Name of Report to Council		
	SGCI	ISR	LRFP
Target audience	Policy planners, City growth management initiatives, development industry	City Council, strategic growth committees	City Council, senior administration, policy planners; finance, business planning and intergovernmental affairs networks; strategic growth committees
Data source(s)	Capital Budget System (CBS): 10-year Capital Plan	Business unit maintenance management systems, CBS	General ledger (approved operating budget), CBS 10-year Capital Plan
Publication frequency	Three-year document in 2009 with annual updates in 2010 and 2011 – next three-year document in 2012	Every three years	Prior to each three-year budget cycle or as economic conditions warrant
10-year period	2009-2018 (for 2009); 2010-2019 (for 2010 updates); 2011-2020 (for 2011 updates)	2010-2019	2011 update – Oct 2011 2012-2021

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- Carla Male, Corporate Reporting
- Roland Mueller, Treasury
- John Veenstra, Infrastructure & Information Services
- Lyanne Wong, Capital Budget Planning

The project was managed by a steering committee:

- Eric Sawyer, Chief Financial Officer
- Beng Koay, City Treasurer/Director of Finance and Supply
- Rick Masters, Manager of Financial Planning, Budgets and Reporting
- Bruce Cullen, Director of Infrastructure & Information Services
- Don Mulligan, Director of Transportation Planning
- Eric MacNaughton, Acting Manager of Transportation Strategy
- Chris Jacyk, Senior Corporate Planner

The project also involved staff at many levels throughout the organization including:

- The Administrative Leadership Team (ALT)
- The Finance & Supply management team
- Project managers from several related corporate planning projects

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