REMARKS TO PUBLIC HEARING ON DNV BUDGET   Jan.12-2002

By J.C. Hunter, P. Eng.

INTRODUCTION:

Good day ladies and gentlemen. My name is John Hunter. I am a resident of Roche Point and a council watcher for about 7 years. I appreciate this opportunity for public input on the DNV 2002-2006 Financial Plan.

I plan to discuss the following items: the new "tax target" formula, the "State of the Nation" (DNV), The Future as I see it, Recommendations for change, and finally a brief summary of my remarks. Detailed remarks on the budget content I'll give in a handout but not speak to.

The Tax Formula

This "tax target formula", adopted last June, calculates an initial target tax increase by adding known cost increases to the increase in CPI – the Consumer Price Index, and subtracts a deemed efficiency gain. It arose, I'm told, because councils historically could not agree on a tax target for Staff's trial numbers early in the budget process. Hence a formula provides the answer Council could or would not.

In my view, this approach is faulty. Firstly, it seems to have become a real target, to the extent that on page C1 we force the tax increase to exactly the 6.91% target, using a small surplus to make the math work.

Secondly, three-quarters of the way through the budget timetable, we are relying on a formula instead of human judgment for our trial budget runs.

Thirdly, the formula does not contemplate potential surprises or political factors that may suggest a different initial target tax increase. The result will be unnecessary recycles.

Let's look at page A2.1. We take the CPI increase from 2000 to 2001 and add a bunch of known cost increases, giving us the $4.3 MM total cost increase. Then we deduct a guess at growth in tax base and a hypothetical efficiency increase.

What's wrong with this? Firstly, why use the CPI increase from 2000 to 2001 instead of a forecast from 2001 to 2002, which is the period under consideration? Secondly, what makes one think that the basket of services purchased by DNV is similar to that purchased by a domestic household which is what CPI reflects? It's apples and oranges.

Third, and worst, you see on page A2.1 the subtraction of terminated programs and their costs. Or do you? Not one program from the last fifty years disappears. Do we seriously believe this reflects either prudence or reality?

Unfortunately, this is typical of the "incremental" budget approach used by the DNV and is a further indication of the cost plus culture.

The State of the Nation

Since the package also lacks the typical "state of the nation" address at the outset, I have written one. You may or may not agree with my version, and my numbers may be off a bit, but here goes:

State of the Nation: Since 1997, while funding capital projects, operating costs, and "capital replacements", we have increased DNV debt from nil to $12 MM, with authorization to $26 MM, and continued to spend both principle and interest of the Heritage Fund. There is little hope of repayment of much of the Heritage Fund withdrawals, such as the $12 MM for the Golf Course. Costs are increasing as residents ask for more services and facilities, and Council keeps approving them, via referenda projects or otherwise. With the ability to sell land when we wanted in the past, we weren't under much pressure to say "no" to projects, but that is changing.

Last year, large new costs characterized as "unexpected" could have forced a tax increase of 15-20%. We were able to reduce that to single digit by depleting the Heritage Fund again, but this time we were also forced to deplete several reserve funds. Our ability to handle further surprises in future is quite limited.

The Future

Unfortunately, our financial situation and flexibility are deteriorating for a number of reasons:

- Over 70% of surveyed residents have told us that they want less than 1% growth in Seymour (including growth on Band lands), and then only after the transportation problems are fixed. Fifty percent wanted none! We can't keep selling raw land in Seymour. Our easy funding is drying up.
- Residents now realize that "capital replacement" is a fancy word for "major maintenance costs", and many object to using the Heritage Fund to pay operating and maintenance costs. Selling fixed assets to pay such costs is viewed as – and is - bad business.
- People are realizing that our Annual Report chart showing DNV in the middle of the GVRD pack in taxes is misleading, because it is per capita. For a typical $400,000 home in DNV, we are the highest taxes in GVRD (page A.7), higher even than West Vancouver, and this chart shows only part of the problem, because it omits utilities. Utilities are about 30% of our total budget.
- Our reserve funds were the lowest in GVRD some years ago, on a relative basis, and may well be worse now, after depleting them last year to stave off a big tax increase.

- Council has asked the Citizen's and Finance Budget Advisory Committee to look at PPP, privatization, and commercialization to generate savings or revenue, but judging by Seymour Water, this may not be well received even if applicable.
- The future cost of maintaining capital infrastructure is estimated by Staff at $11 MM/year. We are funding $2 MM from the Heritage Fund (selling assets to pay maintenance), and $4.5 MM from tax levies. There is no allowance in the budget for the $4.5 MM deficit, which would drive the 6.9% tax increase to about 17% if funded from taxes.
- There is also no allowance for the $745,000 of unfunded budget requests in section C, or the $5 MM of unfunded capital projects in section E of the package (and that assumes Translink puts $ 3.8 MM into the Dollarton Bridge, otherwise we are short $9 MM).
- There is no allowance for the $3 MM to fulfill our guarantee to purchase the North Shore Winter Club, if it defaults on its loan.
- At last valuation (DNV 2000 Annual Report), participants have an unfunded actuarial liability of $548MM in the pension fund for BC employees and to which DNV employees belong. We have no reserve should future top-up be required for DNV's share.
- We have no reserve for any liability re leaky condos, nor any of the many things for which we are jointly and severally liable with GVRD.
- We continually get hit by upward budget "surprises", often over $ 1 MM, (such as the RCMP last year). There is no allowance for such surprises.

Covering the known but unbudgeted costs plus the $4.5 MM unbudgeted infrastructure maintenance costs listed above would raise the tax increase to the 17-20% tax range or higher. This ***<u>excludes</u>*** "surprises" and the NSWC. Our ability to "bury" such increases is much more limited than in past years.

The general public is unaware of the overall situation, and the previous artificially low tax increases (compared to our real costs) sent the wrong messages, in my view. The public may think we can afford everything and that "all is roses".

<u>Well, What Can We Do Now?</u>

As to process, I have four recommendations for Council:

1) **<u>Core review</u>**: Do a core review (zero base) as I recommended previously, department by department, on a surprise rotation basis. Your Citizen's Finance & Budget Advisory Committee also recommended you consider this almost two year's ago. You already do it for the small items such as North Shore Community Grant Applications!

It would be amazing if we could not cut several million dollars from a nearly $100 MM budget. It is not rocket science, the data is available (it has to be to build the budget bottom up; you just review it top down and check assumptions and cost make-up).

This is not micromanagement – Council just set and control the process; independent experts do the actual review with Staff. As to concerns expressed by two councilors, it no more shows distrust of or suggests incompetence or bad faith on the part of Staff than having policies on expense accounts or an internal auditor.

Here's an example from BC Hydro in the paper this week. By reviewing the assumptions behind their plan – which zero basing causes if properly done, they cut $4 MM from one department's budget in one move alone.

Cost plus is from the last century, but it is DNV's culture and methodology. We can't afford it any more.

2) **Peanuts and Elephants**: I suggest Council stop arguing about flower beds and sidewalks and items under $100,000 ***during the budget process***. That ***IS*** micro-management, and leaves you no time to address $90+ MM of the budget. Focus on the big dollars, not the peanuts, at budget time. Create a holding jar (reserve fund) for peanuts and sort it out later.

You cannot delegate review of $90 MM entirely to Staff and fulfill your duty as Council.

Doug Mac Kay Dunn said some time ago at Council: "if you don't understand it, you don't vote for it". I respectfully suggest on that basis that you cannot vote on a $100 MM budget having really reviewed perhaps 5% of it.

If you were tight on family finances, would you look only at your family's proposed spending increases for next year, and ignore the makeup of your base costs which is 95% of the total? Not likely! Yet, that is basically what this Council does. We argue the peanuts and ignore the big dollars.

3) **Revenues:** Have your Citizen's Finance & Budget Advisory Committee look at PPP and the like, but go for the low hanging revenue fruit ***now***. I'll give a very few examples, ranging from large to small:

Increasing the rate of return on district land from the current 1 percent to, say, even a modest 5% would contribute some $2.5 MM to the annual budget.

Dave Sadler's suggestions re false alarms penalties would add $200,000 dollars if costs were kept low for the program. The police and firemen know of each false alarm – can't the bylaw officer just issue a $50 ticket? Do we really need the 1.6 FTE, an office and furniture, and a permit system as proposed in this package (page C15.5)?

Listen to the Golf Society – they are experts. Why are we the only course hereabouts that ***pays*** course marshals? Sure it's only $25,000, but that is something.

Move to more user fees. The surveys of residents show very strong support. There is big money here.

Revenue increase needs as much attention as cost reduction.

4) **Remember People**. Staff manager's compensation, as in most governments and utilities, perversely can increase if the manager has more subordinates and grows his budget. There is an incentive misaligned with the objective of lowest reasonable cost of service.

Secondly, Staff has a heavy workload, especially given the tendency of Council to defer decisions, with consequent recycles. Staff only has time to work on stuff perceived as high priority to Council.

Thirdly, Staff sees Council debate small budget items for lengthy periods, and spend little time on the other $90 MM. What message do you think they get on the importance of culling the bottom of the budget, despite their best intentions?

Under the circumstances above, is it a surprise that incremental budgeting does not provide the lowest practical cost of service to residents?

Want the process to sing? Change the incentive system. Utilities have done it. I did it at Union Gas in a department of 220 people, and within three years that and zero basing cut 6-7% out of our base budget. It got to the point that I had to push harder to make sure enough money stayed in! Incentives work!

Summary

In summary, I do not think that DNV Council can continue on its previous path. We are reaching a critical junction where we be forced to make huge tax increases, or to violate electors' wishes re development. We cannot continue to spend like this, be all things to all people, and hide the results. Our taxes are already the highest in GVRD for an average DNV house.

Cost plus and incremental budgeting were born in and deserve to stay in the last century. DNV can't afford it any more.

Debate the elephants at budget time, and ***after the strategic plan is done.*** Leave a reserve fund for the peanuts – you can't afford to debate them now, unless they have affects on plans that require answers now. Many don't.

There are pathways to progress, but Council needs to change the culture, and the process. Council frankly needs to develop the political courage to be unpopular to more of the people more of the time. We simply can't afford nirvana. I also suggest Council needs to inform the population candidly of the challenges.

SOME COMMENTS ON DETAILS OF THE BUDGET AND BUDGET PACKAGE

The Budget package

There are some modest improvements in the financial plan package in that there is now some data on manpower, your single biggest cost. That this was lacking previously confirms the very weak cost control culture at the DNV.

However, you still lack information in the 2002-2006 package – normally present in a complete budget package - which hides the issue of staff increases, over staffing, and the causes of staff adds:

- No information on overtime or casuals. Insufficient overtime/casual hours suggests overstaffing with full time personnel vs. cheaper overtime (to some limit) and casuals. The latter two options allow handling of peaks and valleys in workload while avoiding the expensive burden of full time employees. You have no hint of the mix in the package.
- You are given FTE – Full Time Equivalent, not full time and non-full time. Who cares? I suggest you should, because when a department shows 6 FTE, it could be 6 casuals, without full benefits, at, say, $40,000 each, or 6 full time at $40,000 each plus nearly 40% benefits. That is a quarter million dollar difference, and while the cost should show, the reasons tend to be hidden. One can budget additional full time Staff without it being obvious. In fact, from the footnotes on page C7, it is not even clear that the FTE numbers represent bodies.
- Amazingly, you still have no table of Staff adds/deducts and the justification, planned consulting, or current vacancies. All you get is the amorphous FTE numbers.
- There is no breakout of salaries vs. benefits to allow you to judge the magnitude and reasonableness of benefits. A calculation shows librarians go for $65,800 each (page C14.5), and fire department maintenance people for $96,500 each (page C11.7). Is that reasonable in terms of both salary and burden?
- Strangely, although there is some breakdown in Executive Services for the Clerk’s Office, there is neither for the Mayor and Council line nor for the Municipal Manager line. Why?
- In summary, your information on your largest single cost -manpower costs remains very thin. These same points were flagged last year.

Miscellaneous:

There is no allowance for additional library Staff despite opening the Lynn Valley Library.

We have had some improvement in adding prior year's history in sections C and D. Why is it lacking in the important section B – the crucial overview and financial plan? Inclusion of a larger page would mean we do not have to fill two columns in by ourselves.

Worse, why are there still no percentage increases calculated year to year for each row of tables B2,B2.1, C6, etc.? The increase in costs year over year vs. inflation is a key flag of reasonableness. Want to know it? You have to do it yourself. And that is after you yourself fill in the first two columns in some cases.

Where are the current and historical figures for reserve funds, an important asset? You are continuing to draw heavily on these (page B2) – what are the balances? Are they still the lowest in GVRD as they were a few years ago?

Where is the potential cut list? I have never seen a budget that did not have a list of possible cuts for consideration.

Where is the $3MM that is supposed to be coming from VPA funding renewal?

Are we really shutting down Ron Andrews 4 years to re-tile it as indicated (E3.12)? If so, why is there not a staff reduction?

What is the justification to spend $3MM/year on watermain replacement? Cost/benefit analysis?