

MEMORANDUM

To: Regional Chair Emmerson and Members of Regional Council

From: Laura Mirabella, FCPA, FCA
Commissioner of Finance and Regional Treasurer

Date: December 17, 2020

Re: Summary of the Financial Accountability Office of Ontario Report on the Financial Impact of COVID-19 and Municipal Budgets

The Financial Accountability Office of Ontario issued a report on municipal budgets and estimated the financial impact of COVID-19

On December 10, 2020, the Financial Accountability Office of Ontario (FAO), which provides independent analysis to the Legislative Assembly of Ontario, published a report titled, "[An Overview of Municipal Budgets and an Estimate of the Financial Impact of the COVID-19 Pandemic](#)." The report was not commissioned by the Legislature.

The report asks:

1. What was the state of municipal finances before the pandemic?
2. What is the impact of the COVID-19 pandemic on municipal finances?
3. Is the federal and provincial financial support offered through the Safe Restart Agreement adequate to fully offset the impact of COVID-19 on municipal finances?
4. If there is any remaining financial shortfall after the support from Safe Restart, what are the implications for municipal budgets?

The report uses internal estimates and publicly available information prepared on an accrual accounting basis

The report uses publicly available information from the Ministry of Municipal Affairs and Housing's Financial Information Return as well as, "the FAO's economic projections, real time

statistics on the impact of COVID-19, external research and COVID-19 updates from 18 municipalities”. York Region was not included among the 18 municipalities although one of York Region’s local municipalities was included.

The report uses municipalities’ annual financial statements prepared using Public Sector Accounting Standards on a full accrual basis. This permits a direct comparison between municipal financial positions and that of the Province. However, it may also present municipal financial information in a format unfamiliar to many. This is because municipalities, including York Region, present their budgets on a modified accrual basis.

This modified basis looks at the expected cash inflows and outflows and balances the two using the property tax levy. Also, on a modified accrual basis, capital spending is treated as an expense in the year it occurs rather than the full accrual method, which capitalizes and amortizes capital over time. Another significant difference between the two types of accounting is the treatment of debt and reserves. Proceeds of debt issuance, repayment of debt principal, and transfers to and from reserves are excluded from the full accrual budget. These budget-to-accrual differences have the effect of increasing the surplus under the full accrual method.

Municipalities are legislatively required to plan for a balanced budget each year on a cash operating basis, but often record higher accrual-based budget surpluses. For example, in 2018 York Region incurred an accrual surplus of \$519.7 million, but the ending operating surplus (actual) was only \$35.5 million due to the differences explained above.

The report provides an overview of municipal budgets prior to COVID-19

The report compares the municipal financial position to that of the province noting that municipal accumulated surpluses, which is the sum of budget surpluses and deficits, grew between 2009 and 2018. In contrast, the Province incurred budget deficits over the same time with increases in its net debt and accumulated deficit.

The report notes that municipalities held approximately \$31.9 billion in reserves in 2018, including \$1.7 billion of reserve funds that are not otherwise earmarked for specific purposes, which the FAO believes could be available for budget stabilization. York Region’s definition is different from the FAO’s; York earmarks certain reserves, including the newly created Pandemic Management Reserve Fund, for purposes of providing budget stabilization. By the end of December 2020, York Region is expected to have approximately \$262 million in its stabilization reserves, which includes those funded by the tax levy as well as by user rates. Including the new Pandemic Management Reserve, up to \$210 million could be available in the Region’s tax-levy supported and user rate stabilization reserves to help mitigate the financial impact from COVID-19.

The Financial Accountability Office estimates that the financial impact of COVID-19 on municipalities will be \$6.8 billion over two years

The Financial Accountability Office projects Ontario municipalities will incur significantly lower revenues and higher expenses due to the COVID-19 pandemic. They estimate revenue losses of \$4.7 billion over two years, including \$2.1 billion in foregone transit revenue. They also project increased expenditures of \$2.1 billion over two years, with social housing and public health accounting for the largest spending increases. In total, the report estimates the combined financial impact of COVID-19 to municipalities will be \$4.1 billion in 2020 and \$2.7 billion in 2021, or \$6.8 billion in total over 2020 and 2021.

Municipalities have implemented cost saving measures and received Federal-Provincial financial support in response to COVID-19

As a result of the pandemic, the Financial Accountability Office estimates municipalities have implemented approximately \$1.1 billion in cost saving measures in 2020, though they note that municipalities do not all share equally in their ability to reduce expenditure. Saving measures include staffing changes, reduction in services and the temporary closure of facilities and program reductions. The report does not assume any savings in 2021.

In addition, municipalities will receive up to \$4 billion in COVID-19 related financial assistance through the Federal-Provincial Safe Restart program, \$3 billion of which is expected to flow in 2020.

The report expects the municipal financial impact of COVID-19 pandemic to be fully mitigated in 2020 but not in 2021

Municipal cost savings of \$1.1 billion combined with \$3 billion of expected funding through the Safe Restart program should, in the opinion of the Financial Accountability Office, be enough to mitigate the 2020 financial impact to municipalities of COVID-19. However, they note that this is an aggregated estimate and not all municipalities may be able to mitigate the impact.

With respect to 2021, the report estimates the financial impact to municipalities of COVID-19 will be \$2.7 billion. Although there is \$1 billion in further Safe Restart money that is available, program restrictions limit the use of funding in 2021 to first quarter transit pressures only, which are estimated to be \$0.3 billion. Unless provincial program rules are changed, the FAO report notes there will be approximately \$0.7 billion of the \$4 billion in federal-provincial support that municipalities will be unable to access, despite a further \$2.4 billion in estimated COVID-19 related pressures.

To mitigate the financial pressure in 2021, the report notes that municipalities may choose to use one or a combination of the following three measures:

1. Use stabilization reserve funds
2. Implement additional mitigation measures such as increasing revenue through additional taxes or user fees or further reduce spending
3. Reduce budget surpluses or run budget deficits in 2021. The FAO estimates are based on an accrual basis which includes non-cash items such as the amortization of capital assets. However, the legislative requirement remains to have a budgeted balance on a cash basis.

York Region is expected to incur significant ongoing COVID-19 financial impacts in 2021 and 2022

As indicated in the December 17th Memorandum on Financial Impacts of COVID-19, which uses a modified cash basis for accounting, the Region is expected to incur overall costs of \$151 million in 2020 related to COVID-19. The impacts are being managed through the Region's mitigation strategies and through support from senior governments. While the Region is expected to avoid a deficit in 2020 and contribute up to \$63 million to the new Pandemic Management Reserve Fund approved by Council on December 10, 2020, funding is expected to be insufficient to address COVID-19 related budget pressures in 2021 and 2022.

As part of the December 10, 2020 Special Council meeting presentation on the Financial Impacts of COVID-19, pressures were identified totalling almost \$70 million in 2021 and \$45 million in 2022. The pressures represent costs in excess of those expected to be managed within the Region's budget. For example, in 2021 total impacts are projected to be \$151 million, including approximately \$81 million expected to be managed within the Region's budget and \$70 million requiring offsets through the new reserve or funding from other levels of government. This approach would allow the Region's proposed tax levy increase to stay within the 2.96% outlook endorsed as part of the 2020 budget.

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