



## Value-Based Outcomes Review: Findings

Date: November 27, 2019

To: City Council

From: Chief Financial Officer and Treasurer

Wards: All

### SUMMARY

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This report transmits the findings of the recently completed Value-Based Outcomes Review (VBOR), conducted on behalf of the City of Toronto. The VBOR analysis and findings will inform the City's strategy for modernizing our financial decision-making to achieve Council's priorities and long-term financial sustainability.

Toronto plays a pivotal role in the region, province and country. The city is a magnet for immigration and economic growth. It delivers key services that provide enormous regional and national economic and social benefit. Toronto is the fastest growing city in North America and part of the second fastest growing region -- the city grew by 77,000 residents in the last year, and nearly 400,000 over the past 10 years. The Toronto Census Metropolitan Area's Gross Domestic Product (GDP) is comparable to each of the provinces of Alberta and Quebec and represents 18.5% of national GDP. Within Ontario, Toronto and the surrounding area have been responsible for substantially all job growth dating back to 2003.

Over successive terms, the City's finances have been heavily relied upon to meet this growth and accompanying regional demand for services such as public housing, transit and transportation, and social services. As the VBOR highlights, the City does so without contributions towards operating expenses from a regional tax or rate base. This creates a significant pressure on the City to manage. The solutions to the City's unique pressures will require partnerships with other governments, including approaches to fairly fund city services and infrastructure which provide regional benefits.

The VBOR analysed actual spending by City divisions and major agencies from 2015 to 2018 with the goal of finding service delivery efficiencies, improving the value of services, and addressing long-standing challenges that have hindered previous transformation efforts. Funding for the VBOR was supported by the Province's Audit and Accountability Fund. Consistent with the Fund's requirements, the VBOR was used to explore efficiencies while preserving service levels.

In addition to new analysis, the review also validates a number of structural financial risks identified by previous City Managers and Chief Financial Officers. The City has developed a roadmap to address many of these risks through its financial management

and operations modernization strategy, while planning for additional, intentional management to achieve progress over the next several years.

Key risks identified in the Value-Based Outcomes Review:

- Assessment of financial information has been made assuming service levels are maintained.
- The current capital plan is based on a set of assumptions which need to be reviewed. These assumptions include the estimates and timing of capital expenditures in addition to the funding requirements.
- The City must address financial challenges surrounding its 10-year capital plan
- Based on the current state of the capital plan the City faces immediate financial challenges.
- The City's capital plan must address its achievability and affordability. This is driven by assumptions about the amount of capital work the City is able to deliver in a given year and the forecasted cash flow required to fund the capital plan.
- The municipal costs associated with the growth of 170,000 residents from 2015 to 2018 have been managed largely through efficiencies.
- The VBOR identifies transformation opportunities that will contribute to funding growth in the future.

Opportunities identified in the VBOR related to moving the City towards financial sustainability include:

- Budgets and systems which create a true multi-year financial view focused on outcomes,
- Amended accountability for the fiscal plan including ownership of corporate savings and the capital plan,
- Clarity in the roles and responsibilities of City Council, the City's leadership, divisions and agencies,
- Changes which allow the City's leadership to adjust headcount to achieve outcomes within budget,
- Allocating savings to be used for transformation projects,
- Reengineering business processes to maximize the value of investments, and
- Mandated corporate programs across all divisions and agencies to better realize efficiencies and savings.
- In addition, there are opportunities to achieve efficiencies and improve value of services. These opportunities have been categorized by the consultant as: collection and enforcement; productivity; workforce optimization; alternative business models; and, infrastructure and asset management.

Undertaking the VBOR provided the City with additional insights and data. The findings of the review will support the Senior Leadership's commitment to achieve City Council's priorities and directions over the next several years, informed by sound, transparent and accountable financial management.

Actions currently underway to address the City's financial sustainability have been confirmed by the VBOR recommendations, such as modernizing the budget process,

transforming financial systems, improving capital asset management, improving capital planning, exploring alternative service delivery, and improving procurement.

The Senior Leadership will bring forward opportunities identified in the VBOR that require Council authority in the 2020 budget process or later in the Council term as appropriate.

## **RECOMMENDATIONS**

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The Chief Financial Officer and Treasurer recommends that:

1. City Council receive this report for information

## **FINANCIAL IMPACT**

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The Value-Based Outcomes Review (VBOR) identifies efficiencies that will inform the City's strategies to find savings and improve value for residents and businesses.

Data from the VBOR analysis identifies that the City's ability to fund the cost of population growth through efficiencies will not be sufficient without changes to the way the City operates and underlying financial drivers, including capital planning, management and financing.

## **DECISION HISTORY**

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On September 3, 2019, City Council authorized the Chief Financial Officer and Treasurer to receive \$500,000 from the Audit and Accountability Fund to assist in funding the City's Value-Based Outcomes Review.

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2019.EX8.1>

On July 16, 17 and 18, 2019, City Council requested the City Manager and Chief Financial Officer and Treasurer to report to City Council with the findings of the Value-Based Outcomes Review prior to consideration of the 2020 Budget.

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2019.EX7.14>

On March 19, 2018, Executive Committee requested the City Manager to report back on individual strategies and key actions contained within the Long-Term Financial Plan to Executive, as appropriate, following the start of the 2018 to 2022 term of Council.

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2018.EX32.1>

## COMMENTS

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### Findings of the Value-Based Outcomes Review

The Value-Based Outcomes Review: A Fiscal Modernization Agenda for the City of Toronto is included as Attachment 1 to this report. The executive summary of the report notes that the review was conducted for the City of Toronto to provide insight into its recent expenditure trends and forecasted financial position, and to provide a series of recommendations that could assist the City in moving towards a sustainable financial footing, informed by data provided by the City, key operating Agencies, and interviews with City and Agency leaders.

#### **1. The City provides local services with regional and income redistribution benefits without appropriate funding sources**

City services provide regional benefits without commensurate contributions from a regional tax base. Toronto plays a critical role in the regional, provincial and federal economies. The VBOR identifies that Toronto services including public housing, transit and transportation, and social services benefit the region. The demand on these services far exceeds the City's ability to respond, putting additional pressure on Toronto taxpayers without commensurate support from other governments. Toronto is under significant financial pressure due in part to the following:

- Toronto provides 90% of the public housing in the GTA and 27% of total social housing in Ontario.
- Toronto Community Housing Corporation faces significant challenges in maintaining properties and meeting the latent demand in the region, where 100,000 people are on wait lists for social housing.
- Only 65% of the total traffic volume on the Gardiner Expressway and Don Valley Parkway is generated by Toronto residents, with the remainder coming from residents of other municipalities.
- Thirteen percent of all trips on the TTC either start or end outside of the city.
- Toronto has a rate of poverty that is almost 1.5 times higher than the region, 1.7 times higher than the province, and 1.8 times higher than the country.

Toronto's infrastructure and services are used significantly by residents outside the city who do not provide direct financial contributions for their use. This is consistent with the City's acknowledgement of the importance to look to strategies beyond our municipal boundaries, and focus on designing, funding, and delivering services that provide a regional benefit. The solutions to the City's unique pressures will require partnerships with other governments, including approaches to fairly fund city services and infrastructure which provide regional benefits.

In addition, the VBOR identifies that the City's policy responses to income inequality, poverty, and affordability has resulted in a greater role as a service provider and administrator of income redistributive programs than many other comparable municipalities. Although the review does not comment on the City's broad policies, it does identify that as property tax -- the City's primary revenue source -- does not benefit

from income or economic growth, the City should be intentional in how and where it creates, funds and runs redistributive programs, and should consider these decisions against its long-term fiscal sustainability objectives.

## **2. Growth, managed through savings and efficiencies, will not be sustainable without transformation**

The City has controlled costs through annual budget targets, service reviews, and initiatives to modernize government and create efficiencies to produce consistent savings.

Between 2015 and 2018, core City operations saw a cumulative annual growth rate (CARG) of 0.6% and agencies had a real CARG of 0.2% while the cumulative annual population growth was 2.1%. The City managed population growth through savings and efficiencies within municipal operations year-over-year and a minimal reduction in per-capita expenditures over that period. The City has delivered incrementally more service to a growing and changing population by working smarter.

The VBOR presents detailed analysis of expenditure trends for City and agency services and finds that over the next three years, continuing to manage population growth through savings and efficiencies will not be possible without transformational efforts. Opportunities are identified in the VBOR in Attachment 1.

## **3. Financial risk is most acute in the City's capital plan**

The external consultant built a financial model with a focus on the City's cost drivers to identify efficiencies while preserving service levels. To reconcile accounting across the City's budgets, actuals, variances and financial statements, the consultant used "free cash flow" analysis. Free cash flow is calculated by taking all sources of City revenue and subtracting the City's operating and capital expenditure obligations in a given year. The analysis builds in growth in the City's population, inflation and known reductions in provincial funding. Additional details on the free cash flow analysis can be found in Attachment 1.

The VBOR analysis found that over the next three years, from 2020 to 2022, the City is forecasted to face financial challenges in the estimates built into the achievability and affordability of the capital plan. These estimates do not contemplate any expansion of services, service levels, or municipal infrastructure. The estimate represents the challenge that is in front of the City, implies a real pressure on the City's ability to maintain service levels and capital investments, and does not contemplate the impact of potential changes such as to the City's debt policy, service levels, revenue generation, or funding from other governments.

The risk is primarily a result of the City generating the amount of contributions required to the existing capital plan and not relying on reserve as a sustainable funding source. The VBOR describes the risk to the capital plan as two-fold: the ability to achieve what is set out in the plan regardless of available funding, and affordability of the plan itself.

The City's capital spend rate averages 62.5% each year. This is due in part to the approval of projects with insufficient cost/benefit information, allocation of funds before project activities are ready to be undertaken, and insufficient capacity in the construction industry. The City is working to improve its capital planning and delivery to increase the capital spend rate by implementing stage-gating for all capital projects, improving capital asset management, and financial policies and governance.

Analysis by the consultant shows that existing assumptions and estimates in the capital plan are not affordable. The analysis finds when the capital plan is adjusted for historical achievability it becomes affordable.

#### **4. Opportunities to deliver better value**

##### **Structural opportunities**

The VBOR proposes a number of structural changes to address the City's fiscal risks and put the City on more sustainable financial footing, including political and administrative culture shifts to support cross-cutting. Full details can be found in Attachment 1, and are summarized below.

##### *Budget and systems modernization*

- Provide a consistent view of finances across budget, financial statements, and variance reports.
- Focus on results, outcomes, costs and demand drivers to improve analysis of allocative and administrative efficiency, service targets, and service delivery models.
- Create a true multi-year view of the budget, against a consistent baseline, taking into account and planning for population growth, service changes, and future spending increases or reductions, to facilitate effective budgeting.
- Review and improve financial systems across the City so decision-makers have consistent, timely, and accurate information on an ongoing basis, and support the ability to consolidate information quickly and accurately.

##### *Ownership and accountability for the fiscal plan*

- The City would benefit by centralizing responsibility for presenting fiscal impacts across all initiatives, overseeing the capital plan, and instituting a process to vet projects for inclusion in the budget based on their degree of readiness.

##### *Delineation of roles and responsibilities of City Council, City leadership, divisions and agencies*

- Council should be responsible for policy setting and oversight, making informed decisions about trade-offs required to deliver services within the City's resources, delegating operational decisions as long as the City's leadership and division and agency staff are following Council's direction and meeting goals and targets.
- City leadership should be responsible for taking Council's direction and translating them into goals and targets, informing Council of the implications of their decisions, and setting corporate priorities and targets, and ensuring compliance.
- Divisions and agencies should be responsible for meeting Council's and the City's goals and targets. Divisions should have responsibility and flexibility to run their business line as they see fit, as long as they are following direction provided.

### *Staffing flexibility*

- Council could approve funding and desired service levels, and allow City leadership to adjust headcount as necessary.
- The consultant recommends that the City create a corporate process to leverage attrition, manage staffing to the City's overall financial benefit, and consider opportunities related to expansion of targeted programs including voluntary separation. The VBOR proposes that the programs should be focused in those areas where productivity enhancements and technology can reduce manual effort.

### *Allocating savings*

- The City could consider dedicating a portion of funds captured by efficiencies and savings to fund transformation projects on an ongoing basis, rather than being added to the end-of-year surplus, with the remainder of savings continuing to be allocated by Council to priorities. This would provide an incentive to realize savings and discourage maximizing spending to meet the budget set at the start of the year.

### *Business process reengineering*

- For every transformation, especially related to digital approaches and technology solutions, focus on business process reengineering to ensure the City is maximizing the value of its investments and meeting the needs of residents and businesses.

### *Mandated participation in corporate activities*

- All divisions and agencies should be mandated, with strict enforcement, to participate in corporate activities. Where necessary, Council should be more willing to provide explicit direction to agencies, especially in those areas of back-office efficiency where there is the potential to realize significant financial benefits.

## **Individual opportunities**

The VBOR proposes a series of operational changes which, on their own, will not derive fiscal benefit, but will increase the City's likelihood of success in addressing its fiscal risks. In considering these opportunities, the review applied three guiding principles: potential value of impact, feasibility under the current legislative and policy framework of the City and Province, and ability to implement. The VBOR identifies that many opportunities align with findings by the Auditor General and the principles of the City's Long-Term Financial Plan. In some cases, up-front implementation costs would be required. This section summarizes the opportunities identified in VBOR, with further details in the full report in Attachment 1.

### *Collection and enforcement*

- Institute a contract compliance review of all City contracts and establish a vendor management program.
- Move to means testing for universal programs to increase access to services while ensuring those who have the ability to pay do so.
- Recover foregone Development Charge (DC) revenue by amending the DC bylaw.

### *Productivity*

- Introduce and expand the use of emerging technologies such as Robotic Process Automation and Intelligent Automation to ease and accelerate back-office functions; and take further steps to make services accessible through digital channels to enhance customer experience.
- Continue to centralize corporate services and reduce duplication across the City, and expand existing and new shared services to agencies and corporations.
- Expand the Administrative Penalty System (APS) and improve court collections including to red-light cameras and automated speed enforcement.
- Optimize procurement by expanding category management to more categories and mandate it for divisions, pursuing demand management, process improvements, and operating model changes, and fully expanding modernization to agencies and corporations.
- Transfer some operations of City-run childcare to non-profit providers where there is likelihood of savings, dependent upon an effective market for alternative service delivery.

### *Workforce optimization*

- Full scale implementation of a time and attendance system for hourly workers, and implement rostering in demand driven services to better match staff to demand.

### *Alternative business models*

- Run commercial operations on commercial business principles, for example: consolidate parking functions under the Toronto Parking Authority and charge market rates; provide debt-financing for water infrastructure; more aggressively pursue non-fare and non-rent revenues at TTC and TCHC; pursue a new build strategy at TCHC.
- Act as a commercial provider, for example, sell or lease the right to use City assets to host telecom infrastructure.

### *Infrastructure and asset management*

- Optimize infrastructure policy, planning and financing, for example, assign a single owner of the capital plan; conduct regular market soundings on the capital plan; and, implement a coordinated, city-wide approach to evaluate financing and delivery models for all major projects.

The VBOR identified that the City's financial structure, approach and capacity is not well matched with its size, complexity and ambition. This mismatch, compounded with the City's short term fiscal pressures results in significant challenges to the City.

The VBOR highlights the solutions to the City's unique pressures will require partnerships with other governments.

Actions currently underway to address the City's financial sustainability have been confirmed by the VBOR recommendations, such as modernizing the budget process, transforming financial systems, improving capital asset management, improving capital planning, exploring alternative service delivery, and improving procurement.



The Senior Leadership will bring forward opportunities identified in the VBOR that require Council authority in the 2020 budget process or later in the Council term as appropriate.

## CONTACT

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## SIGNATURE

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Chief Financial Officer and Treasurer

## ATTACHMENTS

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Attachment 1 - Value-Based Outcomes Review: A Fiscal Modernization Agenda for the City of Toronto