

Subject: Municipal Price Index Feasibility Review

File Number: ACS2023-FCS-FSP-0015

Report to Finance and Corporate Services Committee on 3 October 2023

and Council 11 October 2023

Submitted on September 21, 2023 by Cyril Rogers, Interim General Manager and Chief Financial Officer, Finance and Corporate Services Department

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Ward: Citywide

Objet : Examen de faisabilité de l'indice des prix municipaux

Numéro de dossier : ACS2023-FCS-FSP-0015

Rapport présenté au Comité des finances et des services organisationnels le 3 octobre 2023

et au Conseil le 11 octobre 2023

Soumis le 21 septembre 2023 par Cyril Rogers, Directeur général par intérim et chef des finances, Direction générale des finances et des services organisationnels

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Quartier : À l'échelle de la ville

REPORT RECOMMENDATION

That the Finance and Corporate Services Committee recommend that Council receive this report for information.

RECOMMANDATION DU RAPPORT

Que le Comité des finances et des services organisationnels recommande au Conseil municipal de prendre connaissance de ce rapport.

BACKGROUND

At its meeting of March 1, 2023, Council approved the following motion ([No. 2023 - 09/17](#)) that directed the City Treasurer to “*prepare a report to determine the feasibility of developing a Municipal Price Index for the City of Ottawa.*”

The purpose of this report is to report back to Council on the staff research conducted and provides staff’s recommendation and findings on the impediments with developing and implementing a Municipal Price Index for budgeting purposes.

DISCUSSION

Municipal Price Index Definition

A Municipal Price Index (MPI) measures the yearly change in the cost of providing municipal services. It is used to quantify the difference between costs to provide municipal services and those experienced by the general consumer, as stated through the Consumer Price Index (CPI). The typical costs considered within a MPI are related to labour, construction materials and contracted services, and in contrast, CPI factors costs such as shelter, food and transportation. It can also be used to relate a city’s taxation levels to inflation.

MPI Development

There are various methodologies that can be applied in constructing an MPI. Building a MPI fundamentally includes components of selecting which municipal costs make up the basket of goods, establishing a base year in which MPI levels are measured against, defining cost categories, and calculating their weightings.

Best practice recommends that inflation factors are updated annually and through an independent body. The annual update validates each year’s calculation is congruent with the inflationary pressures for that year and ensures transparency in the process.

MPI Benefits

Potential advantages in using an MPI are:

- Paints a comprehensive picture of pricing changes that impact the range of a municipality’s spending;
- Assists in justifying or explaining increases in annual budget expenditures;

- Illustrates expenditure trends;
- Makes inflationary price fluctuations more visible to provide a basis for purchasing decisions (e.g., managing inventory levels);
- Is more relevant than referring to a CPI;
- Measures the impact of inflation on a municipality over time.

MPI Limitations

Potential disadvantages in using an MPI are:

- Requires a considerable amount of resources to develop and maintain;
- Selects the basket of goods and services is to be fixed and relevant which is conflicting as purchases undergo shifts due to various external factors (e.g. the substitution effect in which consumers will use alternate goods or services when prices escalate);
- MPI is not a standard index and is not in widespread use;
- Its perception of being a self-serving indicator as most MPIs are developed by the municipality using its own methodology.

MPI Use in Other Jurisdictions

The following are some examples of other municipalities' experiences implementing a MPI:

Calgary

Calgary began its use of a MPI in 2003 as it recognized that the CPI was not representative of a municipal purchasing experience. Calgary developed its MPI as a means "to improve the accuracy by which local government costs can be projected" and "creating an understanding that the patterns of local government are quite different than those of an average household."¹ As its MPI development progressed and its use as a tool in the budget process increased, criticism came forward making note of the MPI disadvantages referenced above. In turn to mitigate its opposition, Calgary recommended the following:

- Continuous calculation refinement;

¹ "Developing a Municipal Price Index", City of Calgary [Municipal Finance \(calgary.ca\)](http://calgary.ca)

- Educate council members;
- Publish MPI regularly;
- Maintain longer term views of its finances.

Edmonton

Edmonton first introduced the use of a MPI in 2009. Like Calgary, it noted the best practice to continue calculation refinements by routinely reviewing inflation factors. In addition, to counter criticism of MPI use to be self-serving to the municipality it suggests being transparent and to use external resources. Edmonton also noted its development of the MPI required the creation of steering and working committees. In addition, Edmonton also noted that the use of MPI “is not a prescriptive tool that mandates operating budget expenditures to increase by a designated amount each year. Rather, MPI is a tool that helps better inform the City’s budgetary process of external economic conditions that the City is exposed to.”²

Dryden

The City of Dryden implemented a service delivery and organizational review in November 2020, and created a MPI for use starting in 2021. It identified steps to its creation of a MPI, inclusive of conducting periodic reviews, regularly publishing results, and having third-party reviews. The municipality also cautioned that relying too heavily on a MPI for budget and property tax purposes could incur criticism from residents.

City of Ottawa’s Historic Use of MPI

At the Council meeting held on September 26, 2007, a motion was passed that the City Treasurer prepare a municipal price index for the 2008 budget and that the methodology and appropriateness be reviewed by the Auditor General. On November 26, 2007, the staff provided a report to Council describing the methodology and construction of the MPI. Per the motion, the Auditor General subsequently reviewed the methodology and the appropriateness of an MPI. The Auditor General’s key finding and recommendation was that a MPI should be used with extreme caution given the discrepancies in the calculation of the MPI in 2006 and 2007, in addition to the limited information available for a 2008 projected index. The Auditor General also recommended the use of an independent, specialized third party to validate the City model that was estimated to cost \$100,000. The Auditor General noted that the MPI is not a standard index and there is not an established or recognized model for its

² Municipal Price Index Backgrounder (2023 Update), City of Edmonton [MPI Backgrounder \(2023 Update\)](https://www.edmonton.ca/municipal-price-index-backgrounder-2023-update) ([edmonton.ca](https://www.edmonton.ca))

calculation and therefore could not comment on the validity of the model. In addition, it was noted that the use of an MPI is not a common practice in municipalities across Canada and Ontario. The staff report to Council report identified MPI as a theoretical exercise that can be an important management tool but that should be used with caution and should not be used to incorporate inflation into the budget process.

A subsequent motion was approved by Council on August 28, 2008 as follows:

WHEREAS there is disagreement between the City Auditor and Finance as to how a MPI should be calculated, and

WHEREAS it would require an independent, specialized third party to validate the City model; and

WHEREAS reviewing the audit results will consume both CAWG and City staff time, and

WHEREAS Council does not use the MPI for decision making purposes;

BE IT RESOLVED THAT the calculation of MPI be discontinued and that the 2007 Audit of MPI not be referred to CAWG for resolution.

City of Ottawa's Current Practices

The City completes extensive reviews of its inflationary pressures for the development of its annual operating and capital budgets, as outlined in the 2024 Budget Directions report ([ACS2023-FCS-FSP-0011](#)). Inflationary pressures on contracts and goods and services are reviewed and aligned to negotiated contract increases where known, and other components are based on historical trends or current market pricing increases. Some examples of this are as follows and further depicted in table 1:

- Compensation and benefits are approximately 48 per cent of the annual budget where actual inflationary pressures are aligned to the negotiated collective agreements and benefit contracts;
- Utilities are aligned to actual guided inflationary increases; and
- Contributions to capital (PAYG) are aligned with construction price indices per Stats Canada.

Whereas food is not a typical municipal expense, the City recognizes it provides funding to various organizations that purchase groceries in support of the community and a growing number of these organizations are facing increased pressures as food inflation

risers impacts residents. Staff are factoring a food CPI of 8.5 per cent in its development of the 2024 budget.

The City's current practice of identifying inflationary pressures based on negotiated contract increases, historical trends and current market pricing would provide a more accurate budgetary estimate whereas using a MPI or other inflationary index to develop an annual budget would not be sufficient to meet all requirements or be cost effective. The application of a MPI or other inflationary index to develop the City budget would present challenges as indices are specific to established commodities that would not fully represent the range of commodity and services costs incurred by the City.

Table 1: 2024 Inflationary Rates

Expense Type	Draft 2024	Approximate Percentage of Budget
Compensation / Benefits	2% / 6%	48%
Contracts & Property Leases	2%	2%
Electricity	3%	1%
Heating	16%	1%
Water	2%	1%
Fuel	8% decrease	2%
PAYG	3%	15%
Food	8.5%	N/A

FINANCIAL IMPLICATIONS

The financial implications are outlined in this report.

LEGAL IMPLICATIONS

There are no legal impediments to receiving the information in this report.

ACCESSIBILITY IMPACTS

Finance and Corporate Services adheres to the requirements of the *Accessibility for Ontarians with Disabilities Act, (2005)* in its operations, programs and initiatives. This report is administrative in nature and has no associated accessibility impacts

TERM OF COUNCIL PRIORITIES

This report supports the City's ongoing commitments the current Term of Council Priorities of: a city that has affordable housing and is more livable for all; a city that is more connected with reliable, safe and accessible mobility options; a city that is green

and resilient; and a city with a diversified and prosperous economy. The report also promotes the City's commitment to financial sustainability and transparency.

DISPOSITION

Staff will continue to develop the 2024 draft budget using the City's current practices as further described in this report.