

# City Manager's Budget Message

## 2011 Proposed Operating Budget

October 26, 2010



To: Honorable Mayor and Members of City Council

The City Charter [Section 42. e] requires the development of an annual budget that provides a financial plan for all City funds and activities for the ensuing fiscal year, and I am pleased to fulfill that obligation with the submission of this draft 2011 Proposed Operating Budget for City Council's consideration.

### Overview

By design, the annual budget process brings us together to focus on the next fiscal year which we consider in the context of the current economic climate and our forecasts for the upcoming year. That's a necessary perspective to bring to the budget but it's also important to understand that the Proposed 2011 Budget is the culmination of years of financial decisions that have shaped City services into what we see today.

As we wrestle as a community with the hard choices facing us in 2011, it may be constructive to view the 2011 Budget as a product of that which has preceded it, and recognize that the decisions that we make this year will lay the groundwork not only for 2011 but for years to come.

### Budgetary Confinement

Stability, continuity and sustainability are highly valued attributes in City services and our budget upholds those commitments to our residents. Responsiveness and progress are equally important City service values yet the stagnant economy has bound-up City budgets to such an extent over the last 5 years that little change in our operating services has been possible from year to year. Consistent with that trend, the Proposed 2011 Operating Budget admittedly falls short of our aspirations for new initiatives in City services.

Stability versus change is a choice that each community faces and we use our public processes to help us define where we as a community line up along that continuum. What is troubling is that the budgetary resolution to this dialogue should be decided strategically rather than as a consequence of economic distress. Too often in the last 5 years we've had to take no action by economic default.

The economic reality of the day has forced a retrenchment in many critical service areas and it has taken with it any hope for new programs or expanded services. In the shadow of economic uncertainty, many of our services have been backed into corners where we do our best to acknowledge new needs and wait anxiously for an economic recovery to restore some flexibility in our finances. Until then, we hold the line knowing that doing something is better than nothing, and we continue to work hard to manage the frustrations that this economic stranglehold has imposed on residents, policy makers, and the staff.

The budget message last year was that Kent was "less worse" than most of our peer cities in Northeast Ohio and the same could be said for 2011. Twelve months later we are still in slightly better shape financially than many of our sister cities but the bar has been lowered across the board and although we remain buffered by the economic contributions of Kent State University, the economic problems seen throughout Northeast Ohio during the past two years are evident in Kent.

The housing and mortgage troubles that besieged many of our neighbors has affected our community. Property assessments are down and income tax receipts have slipped. In light of these challenges, City Council has expressed in clear terms its concern for the community's ability to shoulder additional cost for local municipal services at this time and despite revenue decline, we've honored that objective in this budget.

We recognize that in times like these families work to stretch every dollar of income and the City government must also find ways of doing more with less. We continually review priorities, make decisions about what we can afford and what we cannot afford, and seek out better, less expensive ways to deliver essential services. We have done all of those things in preparing this budget just as we have in each of the budgets preceding it.

#### 2011 Budget Strategy

The challenge then for our organization is to prepare a budget for 2011 that recognizes the current stresses felt by many of our citizens without negatively impacting the organization's ability to consistently serve the public now and in the future. We believe we've accomplished that objective through the combination of a very tightly constrained Operating budget and a strategic, and comparatively aggressive, Capital Plan.

One important way to reduce the tax burden on Kent residents is to obtain every available dollar of federal, state, and regional funding. City staff have diligently researched what funds are available and aggressively sought to bring those dollars home to Kent. Between our strong relationships with federal, state, and regional representatives, the support of our partners, and the expertise of our staff, we have been successful in obtaining grants and stimulus funding of over \$40 million dollars over the last 2 years.

Those new funds have injected a degree of flexibility not previously available to us which when combined with our other relatively healthy one-time cash balances (undesignated fund) have enabled us to temporarily bridge the Operating budget shortfalls. In other words, we have leveraged our more liquid funds to fill gaps and hopefully be a catalyst for the eventual restoration of the Operating budget revenue sources.

To that extent, we've worked hard to avoid letting our community goals be held hostage to the economic tide and I think it's working. There is solid evidence in our community that while we've braced ourselves for short term economic stress with a constrained Operating budget, the strategic investments of our one-time funds have begun to make a difference. If the City, Kent State University, and the community continue partnering fully and enthusiastically, I believe we will be positioned to emerge from the great recession stronger than we've been in decades.

Even as our confidence has been tested, we can see evidence of a resilient entrepreneurial spirit that is alive and well in our community as business development continues in our downtown and in other pockets around the City. Businesses, community

groups and citizens are looking for opportunities to partner with the City in efforts such as neighborhood planning, community policing, beautification, and code enforcement. These signs of renewed engagement hold promise for the future of our community that we create together.

In a year when we are proposing to use undesignated fund balance to back-fill our Operating revenue shortfalls, I think it's important to reference our fiscal resiliency. On paper, the City's undesignated fund balance will make an estimated \$3,000,000 contribution to the Operating fund in 2011 – the majority of which, \$2.3 million, is in the utility funds. At that level of investment, the undesignated fund balance will drop to a new balance of \$7,500,000.

It's worth noting that we projected a comparable level of investment from the undesignated fund balance in the 2010 budget but it looks like we will need something closer to \$1 million at year end. I don't want to understate or overstate the use of undesignated fund balance but it's important to recognize that we can estimate 18 months out but we cannot predict – which means we take a very conservative approach with our estimates and we have historically beat our estimates by as much as 30% to 50%. We assume that it is always better to be prepared than to be surprised, and our budget figures reflect that preference.

The undesignated fund balance is made up of previously budgeted funds that were approved by City Council to be spent in prior years but the staff was able to avoid those expenses, and in turn those savings are now available for unexpected needs that arise. Thankfully, previous City Councils and City staff had the foresight to set aside those funds long before anyone had ever heard of the great recession and that act of fiscal responsibility is what has enabled Kent to avoid the kind of employee furloughs, layoffs, and dramatic cuts in services that so many of our peer cities are struggling with today.

But just because we are needing to use undesignated funds does not mean that we take them for granted. On the contrary, undesignated funds remain a revenue source of last resort. Below is a list of the types of fiscal vigilance that we will continue to use in 2011 to minimize any use of undesignated funds:

- We will track and forecast revenues and expenses utilizing historical and month-to-month trend analysis;
- We will monitor and work with our elected delegations to mitigate any legislative initiatives that could threaten our fiscal stability or impose more unfunded mandates on the City;
- We will research best practices in our industry and adopt productivity and cost savings measures wherever practical and affordable;
- We will collaborate and partner to lower our costs and take advantage of economies of scale;
- We will press for State and Federal funds for capital projects through the leadership of our delegation members and any appropriate and available competitive grant processes.

Productivity improvements, efficiencies and cost savings remain a top priority at every level in the City organization. We're as proud of the \$1,000 savings from switching paper vendors, as we are of the \$26,000 in health care reinsurance bid savings. In 2010 we made changes in certified mail, phone service contracts, stop loss for our health plan, printer and copier contracts, and we piloted a new online auction for surplus city equipment. The result was savings approaching \$100,000 above and beyond the

\$141,000 that we cut out of the Operating budget in 2010. That's nearly a quarter of a million dollar swing in the last 12 months which when added to the cuts and savings made over the last 6 years takes the non-personnel savings total to \$2 million – with personnel savings at \$3.5 million.

### Budgetary Assumptions

As reported by Dave Coffee at the October City Council Committee meeting, we have applied conservative budget preparation principals to our initial budget draft, consistent with common practice in most governmental budgets. The most significant budgetary assumptions built into our Proposed Operating budget include the following:

- Most Operating Revenue categories will be flat;
- Operating Expenses in the Operations & Maintenance categories are to remain at 2010 levels except where there is substantiated variance on essential materials or contracts;
- Operating Expenses in Personnel Services have been budgeted at the top of the range for each position (includes 2.5% contractual increases) along with assumption of previous payout patterns for sell back of sick leave, vacation, comp time, and an additional amount for the DROP programs (\$211,000);
- 73.3% of full time City positions are covered by a collective bargaining contract;
- 76.6% of salary/fringe expenses are covered by collective bargaining contracts;
- Variance between top of range budgeting practice and actual for FY2011 is approximately \$490,000 citywide;
- Budgeting for vacant positions totals approximately \$320,000 citywide;

By way of explanation, the practice of utilizing such conservative assumptions for personnel budgeting is to provide the City with a safety net for unanticipated and variable personnel expenses. The City has a relatively high proportion of personnel at the top of their pay range which leaves some budget centers with limited or no tolerance for variances. Variances occur due to termination payouts, personnel re-assignment to different budgetary centers, overtime, special pays, and timing of pay events taking place near fiscal year-end. Conservatively biased estimates tend to immunize us against negative variances that would increase our risk of budgetary audit citations.

One such unexpected variance could turn out to be health care. While we've been able to hold down our health care fixed costs (even decrease them slightly) the wild card is the impact of Federal health care reform. Since the Federal initiatives have taken away calendar limitations and lifetime limitations in health plans, and extended the definition of adult dependents, it is quite possible that our claims may increase. How much and how soon, we can't predict, which is why we take an intentionally cautious approach to forecasting our personnel needs for 2011.

Budget forecasting is not a science but it is research driven. In preparing the 2011 budget we have conferred with our peers and reviewed regional, state and national trend data to help us make educated assumptions moving forward into 2011. Obviously we are not alone in the financial challenges that we face and we think there are lessons to be learned from other cities. Here is a sampling of findings from surveys of other cities that offer some perspective on our relative financial condition:

- The National League of Cities reports that 9 out of 10 finance officers state that their cities are less able to meet fiscal needs in 2010 than in the previous year;
- As finance directors look to the close of 2010, they report declining revenues for the fourth year in a row, ranging from 3% to 4% below prior year;
- Most cities ended 2009 with year to year expenditures outpacing revenues;

- Fiscal pressures confronting cities include declining local economic health, public safety and infrastructure costs, employee-related costs for health care, pension, and wages;
- To cover budget shortfalls, cities are using reserves to balance annual budgets, making personnel cuts, delaying infrastructure projects and cutting basic city services;
- Ending balances of reserves, while still at high levels, decreased for the second year in a row as cities used these funds to weather the effects of the downturn.

The City of Kent is showing signs of many of the same symptoms reported by the National League of Cities, but fortunately, we are less worse than most, and our budgetary recommendations reflect that distinction.

### Budgetary Objectives

The principle role of City Council in the budget adoption process is to ensure that the City's policy commitments are in alignment with budgetary allocations. Have we appropriated the funds necessary to achieve our community priorities?

To that end, the budget is the most important policy action that we will take all year long. It's our investment plan for progress toward the vision we share for our community and for which Kent is proud to be known. Despite diminished resources, this budget will still push for progress on the City's strategic priorities. We will look to partner with our citizen advisory boards, commissions, peer governments, and of course, the public to fulfill our strategic goals as noted below:

- Financial Health and Economic Development  
"to be a prosperous and livable city for all citizens"
- Natural Resources  
"to protect and promote the City's natural resources"
- Quality of Life  
"to enhance lifestyle choices through physical and social environment"
- Community Safety  
"to be an exceptionally safe city"
- Communities within the City  
"to strengthen the quality and enhance the value of neighborhoods"
- City / University Synergy  
"to expand collaborative opportunities that enrich the community experience"
- Governmental Performance  
"to provide the best services at the lowest possible cost"

### 2011 Budget Numbers

I'm proud to point out that the staff came in under the expense budget in 2009 by 12.64% (\$5,124,637) and through 8 months we are tracking to stay under budget for 2010 as well. As a result, for 2010 we had expected to need over a \$2 million contribution from the undesignated fund but it appears that number may be closer to \$1 million at year end – which would leave a balance of approximately \$10,500,000 in undesignated funds at the start of 2011.

The proposed 2011 budget assumes a continuation of aggressive cost containment. We asked staff to propose more cuts everywhere they could, but we allowed a 1% increase in expense line items where justifiable. Increases greater than 1% had to be accompanied by clear explanation and documentation to be sure they were fully defensible.

Once again the staff rose to the budget challenge and out of 51 departmental line items listed in the Proposed Operating budget, 18 lines requested less than 2010, 22 showed no change, and 11 reflected increases. The majority of the increases fell within the 1% range, which when combined with the cuts, enabled the 2011 budget to reflect a very modest 1% increase (\$77,454) overall in discretionary expenses.

As a service provider the City's largest cost relates to its investment in personnel. In total, it costs about \$68,000 per day to perform City services – and 50% of those costs are attributed to Fire and Police functions. Wages represent 67% of the City's personnel costs, retirement 13% and health benefits 12%.

In 2011, the City will be operating at a staffing level (full time) that is the same as we had 13 years ago (192 employees). Driven by employee contract terms, the Personnel costs in the Proposed Budget reflect a 4.3% increase in 2011. In 2011 we will be entering the final year of employee contracts so it is difficult to predict how the next round of negotiations (2012-15) will play out in light of our difficult financial circumstances.

In 2010, revenue figures have showed further signs of decline, although the pace of decline seems to be improving over the second half of our fiscal year. Following a decade (1999 to 2009) where our revenues grew at an average rate of 1% a year, it appears that 2010 may mark the 3<sup>rd</sup> straight year where revenues dropped in total.

In 2009, 17 out of 24 revenue categories declined, but there have been signs of improvement from 2009 to 2010, so for 2011 the staff is projecting revenue declines in only 8 out of 24 categories, flat revenues in 9 categories, and slight increases in 7 categories – resulting in an overall revenue growth rate of 1% (excluding capital fund sources). For perspective, the categories listed as flat for 2011 contribute roughly 60% of the total revenues, the categories showing an increase contribute 30%, and the decliners contribute 10%.

#### In Closing

Despite the stress of delivering public services in such austere economic times, I am honored to work alongside our skilled City employees to implement our collective vision and I thank them for their hard work and dedication. I am particularly proud of the teamwork that Department Heads have exhibited with one another in charting new ways of going about our business.

I would also like to specifically acknowledge David Coffee, Director of Finance and Budget, John Mockler, City Controller, and the entire Finance Department team for the many hours required to produce a spending plan of this complexity and scope.

As the end of another fiscal year looms, like most citizens of Kent, I am grateful to you, our Council Members, for your many hours of service and dedication to our community.

I submit this budget anticipating good things for Kent in 2011, but whatever next year may bring, I look forward to working with the City Council, our staff and the citizenry to keep Kent strong and its future bright for generations to come.

Respectfully submitted,

A handwritten signature in black ink that reads "Dave Ruller". The signature is written in a cursive, slightly stylized font.

Dave Ruller,  
Kent City Manager