

COUNCIL MINUTES

January 30, 2003

The City Council of the City of Mesa met in a Study Session in the lower level meeting room of the Council Chambers, 57 East 1st Street, on January 30, 2003 at 7:30 a.m.

COUNCIL PRESENT

Mayor Keno Hawker
Rex Griswold
Kyle Jones
Janie Thom
Claudia Walters
Mike Whalen

COUNCIL ABSENT

Dennis Kavanaugh

STAFF PRESENT

Mike Hutchinson
Debbie Spinner
Barbara Jones

(Mayor Hawker excused Vice Mayor Kavanaugh from the meeting.)

1. Review items on the agenda for the February 3, 2003 Regular Council meeting.

All of the items on the agenda were reviewed among Council and staff and the following was noted:

The following conflicts of interest were declared: 4a, 4b (Whalen); 5f (Walters); 5e, 5g (Hawker).

The following items were removed from the consent agenda: 6a.

2. Discuss and consider the following budget-related items:

a. Hear a second quarter status report and discuss Fiscal Year 2002/2003 Operating Budget.

Budget Director Jamie Warner addressed the Council relative to this agenda item. He referred to the January 27, 2003 Second Quarterly Budget Status Report, copies of which were distributed to the Council, and provided a brief overview of the document. (See Attachment) He advised that the actual revenue activity through the second quarter of the FY 2002/03 Operating Budget has resulted in a reduction of estimated revenues for FY 2002/03 and reported a decline in the amount of \$9.5 million below budgeted dollars. He added that sales tax revenues are \$2.8 million under budgeted estimates and said that General Government Impact Fees and Building Permits were down \$1 million for the first quarter of FY 2002/03. He noted that State-shared revenues are projected to be \$250,000 less than anticipated, and that miscellaneous land sales will generate approximately \$3.9 million.

Discussion ensued relative to a series of factors impacting the FY 2003/04-2004/05 Biennial Budgets including, but not limited to, a delayed economic recovery; increased Arizona State Retirement System contributions; growing health care costs; self-insurance fund contributions; reduced sales tax and wastewater revenues, and decreased Charges For Services and Miscellaneous revenues.

Deputy City Manager Debbi Dollar provided the Council with a recap of the City's current fiscal year budget savings, including \$1.1 million in Operating Capital; \$500,000 in General Funds; a potential savings of \$800,000 in service level impacts, and \$5.6 million in savings as a result of 252 vacant positions throughout the City.

b. Hear a presentation on the Financial Forecasting Model.

Senior Internal Auditor Chuck Odom highlighted a Power Point presentation in the Council Chambers relative to the City of Mesa's Financial Forecasting Model. He reported that the purpose of the Model is to provide a comprehensive understanding of the available funding and framework for future budgets; assist in identifying variables causing changes in revenue levels; evaluate financial risk; assess the sustainability of current services, available capital funding, future commitments and resource demands; identify and summarize unfunded service requests, and assist in the identification of parameters for setting financial policy. Mr. Odom also provided brief historical background relative to the Financial Forecast System and discussed the structure of the Budget System, Capital Improvement Program Process, Forecast System Structure, Forecast Considerations and Methods, a Seven-Year Citywide Forecast, and a Forecast Process and Timeline.

c. Discuss and consider the sale of \$22,565,000 General Obligation Bonds, \$50,470,000 Utility Systems Revenue Bonds and \$26,805,000 Highway User Revenue Bonds.

Financial Services Director Larry Woolf, Capital Improvement Program Administrator Anthony Araza and Larry Given, the City's financial advisor, addressed the Council relative to this agenda item.

Mr. Woolf reported that after careful review of the 2002/03 bonding program, staff is requesting that the Council approve the order for the sale of \$22,565,000 General Obligation Bonds, \$50,470,000 Utility Systems Revenue Bonds, and \$26,805,000 Street and Highway User Revenue Bonds through competitive sale to provide funding for specific projects included in the City's Capital Improvement Program. He advised that the bonds represent portions of bond authorizations approved by Mesa voters in the 1987, 1994, 1996 and 2000 elections. Mr. Woolf also discussed voter-approved authorizations, proposed bond sale amounts, projected remaining authorizations, and the City's debt structure.

Mr. Given briefly highlighted the competitive bidding process and explained that the bids will be received on February 26, 2003. He added that he and staff will be meeting with representatives of the City's bond rating agencies in the near future.

- d. Discuss and consider an amendment to the City's Utility Systems Revenue Bond Master Agreement, provided certain debt service coverage levels are maintained.

Mr. Given provided the Council with an overview of this agenda item and reported that staff is seeking Council approval of an amendment to the City's Utility Systems Revenue Bond Master Resolution (Master Resolution). He explained that the Master Resolution currently contains a provision which requires the City to maintain a common debt service reserve fund for all outstanding utility system revenue bonds in an amount equal to the combined average annual debt service of the bonds. Mr. Given stated that the amendment would remove the requirement that the City fund the debt service reserve fund for future utility system revenue bond uses, provided certain debt service coverage levels are maintained.

Mr. Given commented that in an effort to amend the current Master Resolution, the City must provide sufficient reserve fund guaranty insurance policies to meet the reserve fund requirement for all outstanding utility system revenue bonds until their final payment on July 1, 2021. He added that this will require the purchase of an additional policy in the amount of \$15.8 million, at a cost to the City of approximately \$237,000.

3. Discuss and consider the City's Median Islands Street program.

Due to time constraints, this item was continued to a future Study Session.

4. Hear reports on meetings and/or conferences attended.

The following members of the Council provided brief updates on various meetings/conferences they attended as follows:

Mayor Hawker

MAG Transportation Policy Committee Meeting

5. Scheduling of meetings and general information.

City Manager Mike Hutchinson stated that the meeting schedule is as follows:

Monday, February 3, 2003, TBA – Study Session

Monday, February 3, 2003, 5:45 p.m. – Regular Council Meeting

Tuesday, February 11, 2003, 7:00 a.m. – Joint Meeting with Dobson Ranch Association

6. Prescheduled public opinion appearances.

There were no prescheduled public opinion appearances.

7. Items from citizens present.

There were no items from citizens present.

8. Adjournment.

Without objection, the Study Session adjourned at 10:00 a.m.

KENO HAWKER, MAYOR

ATTEST:

BARBARA JONES, CITY CLERK

I hereby certify that the foregoing minutes are a true and correct copy of the minutes of the Study Session of the City Council of Mesa, Arizona, held on the 30th day of January 2003. I further certify that the meeting was duly called and held and that a quorum was present.

BARBARA JONES, CITY CLERK

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Attachment

January 27, 2003

To: City Council

Through: Mike Hutchinson, City Manager
Debbi Dollar, Deputy City Manager
Larry Woolf, Financial Services Director

From: Jamie Warner, Budget Director

Subject: 2nd Quarterly Budget Status Report

Purpose

This updated report provides an analysis to date of the 2002-03 fiscal year Operating Budget. This report will also outline the significant issues affecting the FY2003-04/2004-05 biennial budgets.

Background and Discussion

City of Mesa 2001-02 Ending Fund Balance

The budgeted ending fund balance for FY2001-02 was forecasted at \$43.1 million. The actual ending fund balance for FY2001-02 is \$45.4 million.

City of Mesa 2002-03 Forecasted Expenditures and Revenues

The FY 2002-03 Operating Budget assumed a turnaround in the local economy starting in calendar year 2003. Financial activity from July to September indicated a continuation of the recession in the local economy. Consumer spending and building activity were down from budgeted estimates for fiscal year 2002-03. October through December has found a further deterioration of the City's revenue picture. Recent data indicates the economic turnaround will now take even longer to occur which will force more negative estimates to be made for FY 2002-03 projected revenues.

The actual revenues activity through the 2nd quarter FYTD 2002-03 Operating Budget have forced a further reduction of estimated revenues for FY 2002-03 to decline \$8.8 million below budgeted dollars. The 1st quarter estimates had a reduction of \$7.2 million forecasted below, the 2002-03 budget. The City has instituted additional steps to address the greater shortfall as further explained in this report.

Revenues

Sales Tax revenues are down 4.7% to actual receipts FYTD or down (\$2.8 million) from budgeted estimates, (this does not include QOL half cent sales-tax). The new estimate is that sales tax revenue will be at a 4.5% decline in the second half of this fiscal year. Cable service companies have recently received a court decision that excludes them from paying sales tax for cable

services in Mesa. This has been estimated to reduce sales tax revenues by \$336,000 for FY 2002-03. This began December 1, 2002 and will be first reflected in the January receipts. This will put the total estimated decline at -4.7% comparing FY—2002-03 estimated receipts to FY 2001-02 actual receipts. This will place forecasted revenues \$5.7 million less than budgeted for FY 2002-03.

Budget 02-03: \$71.0 million

Forecasted Difference FY 2002-03 to Budget FY 2002-03: (\$5.7 million)

General Government Impact Fees and Building Permits were down 25.5% or \$1.0 million for the first quarter of FY 2002-03 compared to budgeted estimates. There has been a slight improvement through the 2nd quarter and the decline is 22.8% or \$1.6 million compared to budgeted estimates for six months. The estimated revenue for FY 2002-03 will be \$3.6 million below budgeted figures.

Budget 02-03: \$16.0 million

Forecasted Difference FY 2002-03 to Budget FY 2002-03: (\$3.6 million)

State Shared Revenues will be \$250,000 less than budgeted based upon monthly distributions with State Revenue Sharing (Income Tax), coming in \$600,000 less than budget but Auto In-lieu coming in \$350,000 more than budget due to new vehicle purchases. The balance of state shared revenues, (State Sales Tax, HURF, HURF 3%, Mass Transit Assistance), are projected to come in as budgeted.

Budget 02-03: \$121.5 million

Forecasted Difference FY 2002-03 to Budget FY 2002-03: (\$0.3 million)

Miscellaneous Land Sales will generate an additional \$3.9 million with sales to ADOT and SRP forecasted for FY 2002-03.

Budget 02-03: \$ 0

Forecasted Difference FY 2002-03 to Budget FY 2002-03: \$3.9 million

Expenditures

Approximately 252 positions have been identified to remain unfilled for FY 2002-03. This is a combination of unfunded and frozen positions that are forecast to generate a savings of \$5.6 million for FY 2002-03

Refinancing debt payments for General Obligation, Utility and Highway User bonds generated a savings of \$2.7 million for the current fiscal year.

The changes in revenues and expenditures for FY 2002-03, along with a \$2.3 million higher ending fund balance for FY 2001-02 places the forecasted ending fund balance at approximately \$1.8 million less than the budget estimate for FY 2002-03. The Operating Budget is now forecasted to end the fiscal year 2002-03 at \$29.9 million.

Each month the analysis of FY 2002-03 will be reviewed to see if changes in revenue and expenditure forecasts need to occur. This will affect the City's forecasted ending fund balance, which is factored into the FY 2003-04 and FY 2004-05 biennial budgets.

Significant Factors Impacting the FY 2003-04/2004-05 Biennial Budgets

Baseline budget targets for each department in each biennial fiscal year have been distributed. A number of factors will make it more difficult to balance the FY 2003-04 and FY 2004-05 biennial budgets.

Economic Recovery Delayed

As we reported in October, current measures show that the Arizona economy remains in a recession. Approximately thirty six thousand jobs have been lost statewide since March 2001. Statewide retail sales are down 3.3%, through the first quarter of the fiscal year, compared to this same time period last year. Another issue affecting local municipalities has been the competition for retail sales in the valley by the redistribution of customer spending between retail outlets. This can compound the impact in retail sales for specific cities in Arizona. Forecasts are now indicating that a recovery and limited growth in the economy will be delayed until late 2003. A stronger recovery with greater economic growth is forecast for FY 2004-05.

Reduced State Shared Revenues

The Arizona League of Cities has told local governmental agencies to figure on a 16.4% reduction in State Income Tax for FY 2003-04. These revenues are distributed from actual state receipts from FY 2001-02 and will impact Mesa with a decline of approximately \$6.9 million. The State Revenue Sharing for FY 2004-05 has been forecasted to decline by \$1.0 million after discussions with the state on forecasted income tax receipts for 2002-03. This forecast does not reflect any additional reductions due to possible changes in amount to be shared with political subdivisions in the state by the legislature.

Retirement Contributions

The Arizona State Retirement System has sent a draft report indicating that contributions from governmental agencies and participants will have to increase by 110% to recover losses they have experienced on their investments. This increase is forecasted to stay in place for the immediate future. This will result in a \$3.7 million dollar increase on the FY 2003-04 budget if it comes to fruition. The estimated preliminary impact for adjustments in the Police/Fire retirement contributions is projected to have a 59% increase or \$2.1 million.

Health Insurance Costs

Our health insurance consultant has indicated that we should factor at least 11.3% increase in our self-insured health benefit costs for FY 2002-03. This will equate to approximately \$2.5 million more in FY 2003-04. A 15% increase has been estimated for FY 2004-05 that will equate to a \$3.8 million increase over FY 2003-04.

Self Insurance Fund Contributions

In addition, the City needs to consider restoring some level of contributions to the Workers Compensation and the Self Insured Liability Funds. Previous contribution levels for these programs were \$4.6 million and \$1.25 million respectively in FY 2000-01.

Sales Tax Revenue

Since City Sales Tax estimate for baseline budget development was made before the last adjustment downward in forecasted receipts for FY 2002-03, this will have the effect of lowering the revenue estimates for FY 2003-04 and FY 2004-05. Growth factors of 3.2% and 4% are still being projected for the next two fiscal years, but since we are starting at a lower base in FY 2002-03 it will create a reduction in Sales Tax revenue estimates of \$4.4 million for FY 2003-04 and \$4.6 million for FY 2004-05 in one cent Sales Tax revenue.

Wastewater Revenue Estimates

Wastewater residential and multi-family revenues are estimated to be \$1.3million less than budgeted in FY 2002-03. This establishes a lower base for the next two fiscal years revenue estimates along with slower growth rates forecasted from 5% to 3% over the next two biennial fiscal years. This lowered revenue estimates by (\$2.0 million) in FY 2003-04 and (\$2.1 million) in FY 2004-05.

Wastewater and Water Impact Fee revenues were lowered based on receipts to date and forecast activity by (\$0.7 million) in FY 2003-04 and (\$0.9 million) in FY 2004-05.

Charges For Services

Charges For Services revenue estimates have been reduced for Engineering Inspections with the lower forecasted building activity. Some recreational activity is also forecasted to decline over the next two fiscal years. FY 2003-04 estimates are down (\$1.1 million) and 2004-05 estimates are down (\$1.5 million).

Miscellaneous Revenues

Various other adjustments in revenues and expenditures equate to a (\$1.4 million) reduction in FY 2003-04 and a (\$2.5 million) reduction in FY 2004-05.

Conclusion

In summary, these factors for FY 2003-04/2004-05 will create significant restraints on the development of the Operating and Capital Improvement Program budgets. Several factors still need to be determined such as utility revenue rate adjustments, yearly bond sale amounts, adjustments to the Capital Improvement Program, employee salary adjustments and purchased capital needs. We know that the significant items listed above would create a shortfall of approximately \$28 million as a starting point for FY 2003-04. This forecast does not include any adjustments for reductions in state shared revenues that may occur as the state attempts to balance their existing deficit. There are no adjustments for the request from the cable industry for reimbursement for the last four years of sales tax paid for cable services. This has been preliminarily estimated at \$3.0 million.

Over the past two fiscal years, City departments have been forced to cut as much of their operating budgets as possible, without severely impacting service levels. The accompanying report details cost saving measures that have been implemented by City departments in recent months. Most are reflected in the estimates made for the FY 2002-03 expenditures.

The attached budget calendar outlines the remaining budget process and associated key dates.

2002/03 Tentative Budget Calendar

- Jan. 14 - 31 Departments complete CIP O & M for 05/06 - 10/11
 Departments complete Forecast info for 05/06 - 10/11
- Feb. 5 QMST Meeting - Discussion of Roll #1 Budget Submission
- Feb. 6 - 21 Department Budget meetings with City Manager's Office & Budget Office
 Discussion of all areas (biennial budget submission, CIP, forecast)
- Feb. 28 Charter CIP Book submitted to City Council & City Clerk
 (this is not the preliminary book)
- Mar. 14 City Manager's Office sets Preliminary Budgets
 City Manager's Office sets Preliminary CIP
 City Manager's Office sets Recommended Rate Changes
- Apr. 17 Preliminary CIP Book submitted to City Council and Departments
 Forecast Presented to City Council
- May 1,2, 5 City Council Budget Hearings
- June 2 City Council adopts the Tentative Budget
- June 30 City Council adopts the Final Budget and CIP
 Public Hearing on Utility rate changes
- Aug. 1 Utility rate changes become effective

All dates are subject to change. Council hearing dates still need to be confirmed.

**BUDGET STATUS
January 2003**

	Forecasted FY 2002-03
Larger Ending Fund Balance than FY 2002-03 Budget	\$2.3 million
Reduction in One Cent Sales Tax Revenues	(\$5.7 million)
Reduction in Impact Fee/Building Permit Revenue	(\$3.6 million)
Reduction in State Revenue Sharing Funds	(\$0.3 million)
Reduction in Enterprise Revenues	(\$1.1 million)
Other Miscellaneous Revenue Changes	<u>\$1.2 million</u>
Total Changes In Revenues FY 2002-03	(\$9.5 million)
Reduction Personnel costs from 100 vacant positions	\$5.6 million
Higher projected costs for water and wastewater contracts with the City of Phoenix, increased jail costs	(\$3.7 million)
Increase in commodity costs	(\$0.8 million)
Refinancing bond issues to lower debt service payments	\$2.7 million
Capital purchase delays for some vehicles and computers	\$1.1 million
Other miscellaneous changes in expenditures	<u>\$0.5 million</u>
Total Changes In Appropriations FY 2002-03	\$5.4 million
TOTAL CHANGES FROM BUDGETED TO FORECASTED ENDING FUND BALANCES	(\$1.8 MILLION)