CITY OF
MESA
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MESA 2025: FINANCING THE FUTURE CITIZEN COMMITTEE

May 11, 2005

The Mesa 2025: Financing the Future Citizen Committee met in the lower level meeting room of the Council Chambers, 57 East 1st Street, on May 11, 2005 at 4:30 p.m.

COMMITTEE PRESENT	COMMITTEE ABSENT	STAFF PRESENT
Kyle Jones, Chairman	Don Grant	Various Members
Kirk Adams	Robert McNichols	
Jill Benza	Scott Rhodes	
Pat Esparza		
Rex Griswold	EX-OFFICIO MEMBER	
Greg Holtz		
Aaron Huber	Keno Hawker	
Eric Jackson		
Dennis Kavanaugh		
Mark Killian		
Pat Schroeder		
Robin White		

Chairman Jones excused Committeemembers Grant and Rhodes from the meeting.

1. Approval of minutes from the February 23, 2005 meeting.

A motion was made and seconded to approve the minutes of the February 23, 2005 meeting and the motion carried unanimously.

2. Review and finalize Executive Summary.

a. Discuss final report structure.

Chairman Jones reviewed the discussions that have taken place to date among the members of the Committee and said that this evening they were going to start looking at revenue options. He commented that about 60 years ago the City Fathers decided not to have a property tax and instead to use utilities to fund the operations of the City. He noted that times have drastically changed and the City can no longer continue on that path. He added that drastic changes are going to have to be made and said that it is going to take a combination of various income sources in order for the City to achieve its goals.

Budget Director Jamie Warner and Assistant Budget Director Chuck Odom addressed the Committee and noted that the set of revised handouts previously distributed deal with revised figures that staff was directed to put together. He said that the Enterprise Fund, which is the other unrestricted fund balance area, now has an 8% balance and stated that this reflects a $4.8 million a year reduction in the transfer. He reported that the deficit picture for 2010-11 is now just under $135 million. He informed the Committee that staff added the stipulation to serve as the minimum balance goal that the financial advisor and/or bond advisors recommend in order for the City to maintain its bond rating. He added that staff was also asked to develop figures that reflect the “fund all” amount and noted that the numbers were reflected on Page 2 of their handout and averages approximately $132 million a year in additional revenues to fund all General Fund BARs. He pointed out that the 2,000-plus bars are strictly what the departments have identified as needs in the community in the future and have not gone through a review by the City Manager’s Office or the City Council. He said that the total deficit amount for 2010-11 is $754 million. He stated that the last scenario was to determine what the figures would be if they reviewed all of the BARs and select only the items that would fall into the “restoration” category, not new services or the expansion of existing services. He reported that it would require about $35 million a year on average to fund that level of service leaving a deficit in 2010-11 of $175 million. He pointed out that the $35 million would put the City at fund balance goals in 2010-11. He noted that they worked with the various options and those numbers were reported on Page 4 of the handout. (See handout for detailed financial scenarios.)

Mr. Odom reported that the City receives approximately $12,000 a year from water farm leases and added that those figures are in the Enterprise Fund. He noted that the landowners are responsible for the maintenance and the City has approximately 16,000 acres of land in that area.

Discussion ensued relative to the possibility of selling the water to other municipalities, industrial users, etc. to generate a revenue source; a request that staff look into whether State law would allow this to occur; the fact that the Council decided to look at the five-year forecast during the budget roll ups so every time adjustments are made, they are going to take them out five years to determine their ramifications; Ex-Officio Hawker’s opinion that the 8% unrestricted fund balance is a realistic figure and would allow the City to maintain decent bond ratings; the fact that the 3% utility rate increase per year is already built in; the fact that this evening the Committee would discuss the pros and cons of the various revenue types but would not be voting; the fact that staff has not conducted any studies that show what portion of the City’s tax base can be attributed to winter visitors and tourism; a request from Committeemember Killian that staff research this issue and determine what the “export value” is in order to determine (if the sales tax is increased) how much of the burden will be placed on the backs of winter visitors versus full-time residents; and a comparison of sales taxes in place in surrounding communities.

Committeemember Adams commented that if the voters approved the extension of the quarter-cent sales tax, he would like to see how much that would generate, how much would be needed to make sure that the City is able to meet the Proposition 400 match requirements and how much would be left over. He agreed with a comment from Committeemember Griswold that this may be something that can potentially go before the voters and be dedicated to transportation needs, with the priority being the Proposition 400 match.

Mr. Raines responded that the Transportation Division is working on a total update of their plan and the numbers for Proposition 400 reflect that there are $360 million worth of projects that will require approximately $160 million in matching funds over the life of 20 years. He estimated that it would take somewhere between a .25% and .35% sales-tax increase to meet just the match requirements.

Committeemember Killian also requested that staff provide figures that reflect the calculated amount of interest the City is going to pay on the bonds between now and the last year that the bonds go out. He asked whether they could pay the bonds off without penalties and if they can, he wondered if it would be worthwhile to use some of that dedicated sales tax monies to prepay the bonds for the purpose of reducing costs and then converting some of the sales tax monies into direct payments for police, fire, etc. Mr. Raines advised that staff will research this issue and get together with the City's Bond Counsel and Financial Advisory to determine what they can and cannot do.

Committeemember Kavanaugh concurred that they will have to look at a combination of revenue sources, some dedicated and some not, in order to accomplish their goals. He said that if the goal is to be in the neighborhood of 1.8%, he believes they would be competitive as a community (or slightly less). He agreed that a portion of that should be dedicated to the Proposition 400 match for transportation since public transportation and safety are the highest priority needs. He stated that if they look at having a primary property tax he would hope that the voters are asked to dedicate those funds to police, fire and the courts. He added that the portion of the sales tax increase, combined with the property tax, should be dedicated to transit uses because if Mesa does not match the Proposition 400 monies, the funds will go to other communities. He noted that they will still be looking at a number of un-funded BARs in terms of revenue needs but stated the opinion that by dedicating the new revenue sources to some of the priority areas, more traditional monies could be freed up and used for the BARs. He said that it will be important to show the citizens that the City is remaining competitive, that Mesa is still an inexpensive place to live, and that monies are being allocated to the services that they deemed important. He added that they might also seek additional revenues through impact fee areas and pointed out that Mesa does not have an impact fee for roads and other categories. He stated that although this is a controversial area, a majority of Arizona communities use impact fees as part of their revenue package.

Chairman Jones discussed the current Quality of Life tax and said that the first quarter (for ten years) is for capital and the other quarter was for operation and maintenance. He said that although the capital will end, the operation and maintenance portion will continue.

Discussion ensued relative to taxes of food and Mr. Raines reported that the only municipalities in the State that do not tax food are Phoenix, Tucson and Mesa; the fact that placing a sales tax of 1.5% on food would recoup approximately $8.7 million a year; and the fact that Chandler and Gilbert tax food at 1.5%.

In response to a question from Committeemember Griswold, Mr. Raines advised that Scottsdale charges an annual permit fee for service-type industries based on the number of employees and the amount increases incrementally (1 to 5 employees, 5 to 10 employees, etc.). Committeemember Griswold noted that in Mesa, restaurants are the only industry taxed and said he would like other sources to be identified. He added that he would like the legality of that checked into to determine how the monies could be used. He questioned whether the funds could only be used to pay down bonds or whether it would be placed in the General Fund.

Mr. Raines commented that electric utilities are rarely bought and sold in the United States and said that the process would require significant analysis that is beyond staff's capability at this point.

Committeemember Adams stated the opinion that it would be beneficial to have an outside party look at what the value of selling the utility would be. He said that if the utility was sold, he would like to know what the corresponding "drop" in capital expenditures and the money they are going to have to spend to improve the deteriorating infrastructure would be. He added that he is hearing that they are going to have to spend a lot of money on the City's entire utility structure/infrastructure and said that the information will help them determine the value of holding onto or selling the utility.

Mr. Raines responded that he believes the maintenance issues are already taken care of "off the books" in the forecast and said that they are only looking at the general fund allocation, that transfer.

Mr. Warner concurred and said that a lot of the maintenance is already taken care of because they are showing a net transfer. He added that if the City was not going to own any of its utilities, there would be a reduction in bond cost because they would be issuing debt to replace the infrastructure. He noted, however, that they would also lose $70 to $80 million a year in net income that they cannot afford to lose. He advised that the forecast still assumes that there will be a net income transfer and if they are going to assume that they are not going to own a utility, there will be some obvious initial cash upfront on the sell but eventually they would be dealing with a significant shortfall. He reported that the City generates approximately $240 million in gross revenues from the utilities. He added that upwards of $2 million sales tax revenues are generated annually.

Chairman Jones pointed out that although the City would receive the cash up front, those monies will dry up in a few years and they will no longer have that revenue coming in. He agreed that there would be a corresponding "drop" in costs but emphasized that over the long-term, the City will fall way behind.

Committeemember Adams commented that he would like to see all of those numbers so that he has some concrete information upon which to base a decision.

Additional discussion ensued relative to the possible sale of the utilities, sales tax, and revenues.

Committeemember Killian asked what the figure would be if they take the net revenue generated by utilities plus the sales tax generated on the sale of the utilities. Mr. Odom responded that it would be $2 to $3 million a year plus the transfer. Committeemember Killian said that if they sell the utility they are going to have to figure out how to generate $64 million plus $2 to $3 million on top of that.

Committeemember Adams said that his concern is that the transfer is actually an artificial number because they have not been maintaining the infrastructure and they have been told that there are large investments that need to be made in this area. Mr. Raines clarified that they are maintaining the infrastructure but not to the level that they would like to. He agreed that there is some "catch up" that needs to be done and added that they are expanding, there are current on-going maintenance and there's replacement issues as well. He estimated that they are doing about 70% of what needs to be done. He noted that a lot of the infrastructure costs are taken care of in the Enterprise Fund, the transfer.

Chairman Jones referred to a letter contained in the member's packets from Dave Plumb regarding the operation of Mesa's utilities and how they differ from most municipalities because they have relied so heavily on utility revenues and do not operate their Enterprise Fund quite the same, which creates a dilemma. He said that because Mesa relies so heavily on utility revenues, they can not use the typical model.

In response to a question as to whether utilities are sold, whether the City would be "trailblazing" if it did so and if there are possible interested buyers, Mr. Raines stated that he is not an expert in this area and there are probably few in the field. He added the opinion that there is more of a market for gas and electric utilities than there would be for wastewater, water, irrigation, etc. He reported that Mesa's electric utility generates approximately $6 million a year (25-26%).

Discussion ensued relative to the fact that realizing a 20% net on the sale and eliminating future on-going revenues may not be the better route to follow.

Committeemember Kavanaugh commented that after 9/11, safety issues have surfaced such as whether municipalities could trust the running of the utilities to outside entities. He expressed the opinion that the City has some wonderful assets and they need to keep them healthy while looking at other areas of their portfolio where they are not being fiscally conservative. He said that they have good investments with the utilities but they are relying heavily on a risky investment, sales tax. He added that in order to be fiscally conservative, they have to have revenue sources come in from diverse sources, for the conservative side (a property tax) to the more risky areas. He stated the opinion that the City should retain the solid investments they have in utilities but strive to rely less on risky ventures. He added that expert advice will need to be obtained in order to pursue the possible sale of the City's utilities and, in his opinion, they have done a good job in this area, they represent a good aspect of the City's portfolio and he believes they should focus on other areas to strengthen Mesa's revenue portfolio.

Committeemember Schroeder advised that three weeks ago she conducted research on the sale of utilities and the only one she found was in Illinois in 2004 from a municipality. She noted that there is not much of a market for this activity and agreed with Committeemember Kavanaugh that she would be hesitant, from a national security risk, to have outsiders in charge of the City's water. She said that she would prefer to have that handled by a municipality rather than a private company.

Committeemember Jackson commented on the fact that the City of Mesa has not had a property tax in effect for a very long time. He referenced remarks made by Committeemember Killian during previous meetings regarding the importance of ensuring that senior citizens on fixed incomes are not negatively impacted and said that perhaps they could "set a floor" somewhere. He added, that for example, they could implement an assessment for property tax at an assessed value over $50,000, and commented that this approach might be more sellable. He stated the opinion that a property tax would represent a more stable and conservative revenue base. He noted that the large amount of vacant land in the City and said that if the voters approve a property tax, that will spur investment because when people have to pay taxes on something, they don't want to just "sit on it," they are more likely to develop it. He stated that they should consider assessing a property tax on parcels above $50,000 in value on the residential side. He added that he is not proposing that this be done on commercial or industrial properties. He further stated that assessed value is substantially less than market value and has some ceiling on how much it can increase in a year.

Committeemember White also commented on the property tax issue and noted that in British Columbia they have instituted a successful program whereby if someone is living in a house that is the primary residence, the owner receives a homeowners' grant. She noted that senior citizens get a bigger portion of the grant, which serves as a credit against their property taxes. He added that it also means that people who have residential homes that are leased out pay more than someone who is actually living in it. She also agreed with Committeemember Kavanaugh's remarks relative to the sale of the City's utilities and said they should not pursue this matter. She added that a 20% return is a good, healthy one and should be maintained.

Committeemember Griswold pointed out that after 9/11 the City took more money out of the utilities but did not do a lot of the infrastructure repairs. Mr. Odom commented that when they got into the volatile period of electricity pricing, the City did not have a method to recover their cost for electricity. He advised that a year ago October they instituted the Electric Cost Adjustment Fund (ECAF), which has restored the City to their historic levels of profitability.

Committeemember Griswold advised that having a utility run by a political body, such as the City Council, is problematic. He said that during election years they don't raise the rates at all and then the following years they have to increase it 7-8% and the citizens react. He said that although a 20% return sounds great, but if they are straining their "cash cow" and politically the rates cannot be raised anymore, then problems occur.

Mr. Odom responded that the strain has been City-wide and what they are seeing in the utilities' areas is happening throughout the City.

Discussion ensued relative to "debt valley;" the fact that the City's restricted CIP Plan is almost exclusively utilities throughout this forecast; the fact that the City of Page took over their utilities a few years ago, and set up an appointed board that makes utility decisions; the fact that this separated it from the Council, yet it still remains a property of the City and generates revenues; the Committee's desire to have Mr. Plumb address them regarding these issues; the "Phoenix Option," where the City tells its residents what the rates are expected to be over the next five years to avoid "rate shock;" the fact that the City's model calls for a 3% increase per year; and the possible sale of the water farm; property tax estimates; the fact that Mesa does have a property tax that they pay to the County, Mesa Community College, Flood Control, Fire & Library Districts, EVIT and Mesa Public School; the fact that Mesa still has a rental sales tax in place; and the fact that 30,000 acre-feet (enough to support 100,000 people) of water can be pumped out of the water farm; an estimate that the cost is $1.00 per thousand gallons.

Committeemember Killian said that he supports fallowing the ground, selling the water and using it within the utility system. He estimated that this would generate more than the $40 million a year they need. He stated that his concerns with regard to a property tax is that it is not "exportable" and is levied without any relationship to people's ability to produce income. He added that at least with a sales tax purchases can be adjusted. He asked whether any other cities owned water farms and was advised that Scottsdale operates one and uses it as an assured water supply. Mayor Hawker commented that Mesa probably does not need the water farm for this purpose but said that they are not entirely sure about that at this time. Committeemember Killian commented that the water farm represents a huge "cash cow" that should be seriously looked at. He reiterated the importance of determining how much revenue the City can generate as a result of selling the water and whether they can do so legally.

Mr. Warner noted that the other important issue is timing and questioned whether sufficient revenue could be generated by 2007-08 to deal with the debt service cost. He expressed the opinion that selling the water and generating the necessary income by that time would be practically impossible.

Committeemember Killian commented that the Indian communities in that area are expanding farmland at a rapid pace and said that they may be willing to lease land and/or buy the water from the City. Mayor Hawker pointed out that there are transportation difficulties since there is no piping system in place to move the water. He added that trading within the CAP system is very difficult and there are arsenic, salinity and other problems associated with that.

Committeemember Killian noted that water can be banked or trades can be made on the amount of water usage. Mr. Warner further stated that the City must still have the ability to access CAP water.

Additional discussion ensued relative to banking water; the importance of ensuring that the water is tied up and they are unable to sell the land underneath; the fact that in terms of a property tax, the average family would pay between .55 and .65 per day using the proposed figures over the course of a year; the importance of asking the citizens what they would be willing to pay to have the services they want; and the fact that the water farm is an important investment area that will provide revenue, but is not the "end all" for the City's revenue needs.

Committeemember White stressed the importance of getting the expenditures in line and noted that the Committee's Mission Statement is to make recommendations for cuts on the budget and look at new revenues as well as revenue adjustments. She stated the opinion that they are straying from this charge and commented that they have not yet responded to the suggestion received from the citizens at the public hearing that was held.

Jeff Welker, Deputy Building Safety Director, addressed the Committee and said that he has partial responsibility for administering the impact fee program for the City. He referred to a memorandum contained in the Committee's packets and briefly outlined its contents. (See backup materials for specific memorandum details). He noted that as development in Mesa slows, so does the amount of revenue that is generated by the development in the form of impact fees and added that development will slowly diminish and the City approaches build-out. He added that unless Mesa wants to expand the City limits beyond the current plan, build-out will occur in 2025 and, as the City slowly builds-out, the fees and revenues will slowly decline. He also commented on redevelopment and noted that State law requires that the City give credit for what was there before.

In response to a question from Committeemember Esparza, Mr. Welker explained that general government facilities includes buildings such as the municipal building tower or other non-specific buildings. Mr. Welker confirmed that Tucson and Tempe, like Mesa, do not have impact fees for roads and commented that the fees have unique challenges and complexities associated with them. He added that although other types of fees could be implemented, he believes they would be problematic and commented on the fact that Apache Junctions' efforts to institute a school impact fee was challenged in court and thrown out.

Committeemember White commented on the fact that a few months ago she read in the paper that there was to be a new impact fee for museums, the Visitor's Center and the archaeological site by Mesa Lutheran Hospital. Mr. Welker clarified that it was not a new impact fee, the cultural fee has been onboard since 1988. He said that an opportunity came up to increase the fee because assets, values and costs had gone up. He noted that in the end, staff was instructed to move some of those assets that lowered the value and, in essence, lowered the proposed increase and ultimately the increase was adopted. He outlined the facilities that fall under the heading of cultural and said that he would provide the Committee with a copy of that list.

Mr. Welker confirmed that most cities include the cultural fee in the parks area and said that in 1998, when the City was bringing them onboard, the Council felt it was important to separate them and account for them on a separate basis.

Committeemember Killian noted that historically Mesa's impact fees have been lower than the surrounding communities and asked whether the City has "maxed out" on most of them as far as what they can legally do and whether they have just been conservative in this regard. Mr. Welker responded that the question is problematic and said that legally they could probably include some more assets in each of the categories, which would increase the value of the assets (the total asset values) and therefore increase the fee. He stated that they like the fact that most of them are at the maximum limit.

He added that although arguments have been made that the fees restrict/discourage development, if they look around at the fastest-growing cities in the Valley they will find that they have the highest fees. He added that it is a great source of revenue for the City but it's not a never-ending source, it is development driven.

Committeemember White asked whether Mr. Welker anticipated a new impact fee for the new Arts Center and he replied that at this time staff is not prepared to recommend one. He explained that staff views that as a one-time cost and as the City grows, they are not going to build on or expand on growth. He noted that it would triple the fee if they did so. Chairman Jones noted that it was paid by the Quality of Life Tax and was a one-time deal with no debt service.

Mr. Welker pointed out that impact fees for the most part do not pay 100% of the capital costs; they help fund the costs. He added that the greatest potential for 100% would be in the cultural and library areas but noted that this is a rare occurrence. He commented that there is the potential to look at expanding the assets list to be less conservative than they are at the current time. He reported that they would not double their revenue; they would generate approximately $1 to $2 million more a year.

In response to a question from Committeemember Esparza, Mr. Warner advised that both the cultural and library areas have significant fund balances with the Library (04-05) having about $3.6 million at the end of this fiscal year. He added that cultural is scheduled to be spent down a fair amount. He explained that the reason why the library is at that level is not because they don't have the money to build or expand, it's because of the operating costs, which keep forcing those back into the CIP to later years. He said they have the money to build them, but it is the operations that they can't afford that forces them back to later years. Mr. Raines noted that cultural is almost down to zero.

Committeemember White asked about parks and pointed out that the City has not opened a new park in four years. Mr. Raines responded that there is debt on the parks that they have opened and debt on new land that has been acquired but not built on.

Mr. Welker informed the Committee that staff conducts a fee study every two years and said that if they so desire, the Committee could recommend to the Council that asset lists be evaluated more liberally. He confirmed that the developers do not stop building because of higher impact fees.

Discussion ensued relative to the importance of having staff be more vigilant on what they put into the assets and perhaps yield $1 million more a year, which would pay for 25% of the operating costs for the new Arts Center; the possibility of directing staff to look at the possibility of implementing a street impact fee.

In response to a question from Committeemember White regarding expenditure discussions, Chairman Jones stated that during previous meetings he has asked members of the Committee to forward recommendations regarding expenditure cuts that they would like to see in their report. He noted that the report will be all inclusive and noted that not everyone will agree but their input will be reflected.

3. Scheduling of meetings and general information.

Chairman Jones announced that the next meeting will be held at 4:00 p.m. on May 25th.

4. Items from citizens present.

There were no citizens present wishing to speak at this time.

5. Adjournment.

Without objection, the Mesa 2025: Financing the Future Citizen Committee adjourned at 7:16 p.m.

I hereby certify that the foregoing minutes are a true and correct copy of the minutes of the Mesa 2025: Financing the Future Citizen Committee meeting of the City of Mesa, Arizona, held on the 11th day of May 2005. 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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