

May 12, 2014

BUDGET MESSAGE

Honorable Mayor Scrace and Council Members:

In accordance with the provisions of the City Charter, submitted herewith is the 2014-2015 Annual Budget for the Fiscal Year starting July 1, 2014.

INTRODUCTION

The overview which follows contains a number of key points worth highlighting before describing the main points of each of the funds. While this budget balances expenditures with available revenues as required, there are serious economic and fiscal conditions that merit attention.

OVERVIEW

ECONOMIC TRENDS

While the economy has now stabilized, the recent national, state, and regional economic situation greatly impacted the City's finances and will do so for the foreseeable future as municipal governments come to terms with a new normal, a significantly lowered baseline of revenue. The City has been impacted by the trend dating back to 2002 where revenue collected and sent from the State of Michigan to cities had declined, estimated by the Michigan Municipal League to cumulative loss of revenue sharing to the City of Grosse Pointe of \$1.5 million between 2003 and 2013. Even more significant was the drastic decrease in property tax revenue.

Property taxes are the primary source of revenue for cities in Michigan. Due to the strained national and regional housing market, property values declined in Grosse Pointe for six years in a row after a peak in 2006. Cumulatively, this cut values in half for residential properties. Residential values have turned the corner with assessments rising more than 5% on average. This will be the second year without a decline in assessments. However, the City will not experience a commensurate uptick in property tax revenues. The cap on increased taxable

value for any property is the annual inflation rate, under the Michigan Constitution, which is 1.6% in the upcoming Fiscal Year. Grosse Pointe is also prohibited by the Headlee Amendment from raising its property tax rates to levels allowed by its City Charter. On top of this, personal property decreased due to values of \$40,000 or less being exempt from personal property tax. So while the real estate market is recovering, City finances must still face the stark financial task of dealing with property tax revenue levels that have reverted to those found in the last decade, and will take more than a decade from now just to get back to pre-recession levels of 2006.

PROCESS

The Council provided general direction to staff on developing a budget that met the goals of the Council during the preliminary budget discussion in February. With that direction the department heads submitted their budgetary needs and estimates and the draft budget was compiled.

Notwithstanding the increasing expense environment, the Fiscal Year 2014-2015 budget is balanced without dipping into General Fund reserves or increasing the General Fund operations property tax levy (prohibited by the Headlee Amendment without a vote of the populace). No General Fund fee increases are proposed in the upcoming budget. The solid waste property tax levy also remains unchanged (and unable to be increased due to Headlee).

Parking fees remain unchanged. Water and sewer rates are budgeted to slightly increase with the rise of the cost of wholesale water produced by Grosse Pointe Farms and debt service payments from the City wide sewer repair project underway financed by a low cost loan from the State of Michigan. The Capital Projects Fund, which will be tapped for new Public Safety vehicles this year as well as needed building repairs, must also continue to assume responsibility for major street project expenses.

The transmittal of a balanced budget was slightly less challenging than it had been in the last few years. State revenue sharing was down more than 35% since 2001 when payments were about \$227,000 per year higher, but is expected to stabilize and possibly increase in the proposed budget, pending approval in the state legislature. The expected State of Michigan contribution from motor fuel taxes toward the City streets is estimated at \$317,000 requiring the City to contribute nearly \$254,000 to the Highway Fund for street maintenance costs. While revenue sources are significantly limited, there are built-in cost increases to operating City services. Personnel costs are the single biggest expenditure in a municipal budget, and many costs related to employees are rising beyond the rate of inflation, particularly those related to retirees and legacy costs.

While the economy has stabilized and the housing market is rebounding, the underlying fiscal conditions raised above will still create budgetary challenges as expenses that have been put off come due. Unfunded needs to provide for infrastructure improvements and retirement costs continue to skyrocket, upcoming budgets will require priority setting, service level adjustments and changes in the way local government has administered things in the past. With the decline in the equity markets during the major downturn, the pension

system has gone from significantly overfunded of more than 150% before the Great Recession to an estimated 110% in the pension fund at the beginning of the last fiscal year. The City continues to be actuarially required to contribute City funds in the Pension system, albeit at a significantly lower amount this year due to recent investment returns, a contribution projected to rise over the next several years. The most significant challenge is paying for the already promised retiree health care. Premiums for Medicare age retirees increased 11% for 2014 over the previous year. Without replenishment of the retiree health care trust, the General Fund will assume a portion of the cost of providing health care to current retirees in the fiscal year 2015-2016 budget and the entire cost in the 2016-2017 budget year.

The economic trends will continue to create significant challenges which will require creativity and flexibility. The City will continue to examine its health care and retirement related employee benefits, and seek to impose reduced benefit levels on new hires. The City will need to deliver services more efficiently. The City will need to regularly evaluate its level of services to make sure its limited resources are being spent on the services the community desires. The City of Grosse Pointe continues to examine potential options for enhancing public safety service cooperation as we look for ways to deliver fire and police protection, now comprising 59% of the General Fund budget, most efficiently yet at the highest service levels possible given the increasingly limited resources.

GENERAL FUND

The proposed budget as submitted balances revenues with expenditures. Total General Fund outlays are proposed to increase 0.34 % compared to last year. The charts which follow this budget message summarize proposed General Fund revenues and expenditures.

The City's major property tax generator is the general operations levy. The 11.8391 mill general levy is proposed to remain at the same rate for the 2014-2015 budget year.

The City's taxable value for 2014 is estimated at \$326,739,161, an overall increase from last year. Property tax revenue is budgeted at \$3,851,098, an amount \$61,811 higher than budgeted last year.

State Shared Revenues are estimated at \$448,050. State Shared Revenue provides 8.2% of general fund operations.

Overall, the City's General Fund budget is proposed to be \$5.5 million, fairly consistent with the budget in 2013-2014.

Some highlights of changes in this year's budget expenditures include:

- o Allocation of an increased amount of funding for a future year's retiree health care costs in the total amount of \$200,000, including contributions from other funds proportionate to employee costs from that fund (e.g. Parking and Water/Sewer)
- o Increased customer service through the partial replacement of a payroll clerk with an enhance customer service presence within the Finance Department, an increase in the

budget for customer service training, and a reservation of some funding in contingency for potentially identifying technology solution such as a smart phone application to enhance the City's ability to communicate quickly and effectively with the residents.

o Restoring the number of times the City powerwashes the sidewalks in the Village to twice per year as was done prior to the economic downturn.

SOLID WASTE FUND

The revenues of the Solid Waste Levy, which remains at the same tax rate as last year, are allocated in this fund as reserved for only rubbish related purposes. With the reduced revenues from property taxes, very little has been reserved for future equipment purchases. The existing Cushman's are budgeted to be replaced over the next several years which will continue rear yard pickup. In 2013-14, the City combined the commercial and residential pickup schedules to reduce costs, both in capital as well as personnel, and changed to a 4 day residential pickup schedule. Conversion of additional areas in the Village to compactor service as surface parking lots are reconstructed will also help to stretch already reduced manpower.

GENERAL DEBT FUND

The General Debt Fund pays for debt issued by the City of Grosse Pointe Building Authority and also the City of Grosse Pointe. There are two outstanding bond issues: 2001 Building Authority Refunding Bonds for new municipal offices, Council-Court Chambers, and Public Safety alterations expiring in 2014; and 2011 General Obligation Refunding Bonds for the Neff Park swimming complex. Total principal and interest payments for fiscal 2014-15 are \$431,478. The Building Authority Bonds are financed with general operating property tax revenue, while the General Obligation Refunding Bonds receive funding from a voted millage with a dedicated levy.

Due to the increase in the Neff Park Pool principal payment for fiscal year 2014-2015, the budget as outlined increases the debt retirement millage rate by 0.0102 mills. This is necessary to generate the funds to fulfill the debt service requirements, as voted by the public prior to the pool construction. This also allows the City to continue to avoid having the General Fund subsidize the pool project when the demands on the general fund, particularly public safety needs, are so high.

CAPITAL PROJECTS FUND

Capital spending for equipment and building improvement has been pared back significantly from the levels of more than eight years ago. The most significant expenditure is for an operating transfer out for street projects. The Capital Projects Fund also lists all of the City's vehicles and major equipment for the Public Services and Public Safety Departments with the projected replacement schedule in future years. Public Works has moved to a three-year replacement cycle for the City rubbish trucks instead of every two years, and pick-up trucks have moved from an 8-year replacement cycle to a 10-year cycle, or longer whenever

possible. As called for in the City Council's goals, a significant amount of \$100,000 has been allocated to starting catching up on improvements to the interior and exterior of City buildings. These expenditures must be prioritized from a list of more than \$300,000 of estimated projects to fix City Hall, the Public Safety Building, the Public Works Facility and Neff Park. These are improvements that have been delayed during the recent economic turbulence the City has endured. But without a dedicated source of revenue to replace these expenditures, in five years, the Capital Projects Fund is projected to be depleted. Most significantly, there will be no remaining source of the roughly \$250,000 in funds that have typically been allocated to major road repair projects.

WATER SUPPLY & SEWAGE DISPOSAL SYSTEM

The budget projection for the Water and Sewage Disposal System shows total revenue of \$2,554,552 and operating expenditures of \$2,112,651. Operating income is budgeted at \$441,901, along with a projected interest income of \$5,000. Capital outlay for major projects is proposed at \$625,000. This is to replace the water mains on Chalfonte, and also the water main in the Fisher Road business district.

The City's consumable water is supplied by the City of Grosse Pointe Farms and sewage processing is completed through the City of Detroit Sewage System. Readiness to serve charges remain fairly unchanged due to the City keeping its operating costs down. Commodity charges are being increased somewhat by the City of Grosse Pointe Farms which produces water for the City. The Debt service component of the rates will increase due to passed debt issuances, including the full cost of the City wide sewer repair project.

HIGHWAY FUND

The Highway Fund provides separate accounting for all operation and improvements to the City streets. State Shared gas and weight tax revenue and contributions from the General Fund support this activity.

State Shared Highway Revenue is estimated at \$317,000. The General Fund Contribution is proposed at \$253,644 to cover the cost of winter street maintenance, routine street maintenance, tree trimming and removal and capital outlay for crack sealing and maintenance construction. A contribution of \$575,477 from the Capital Projects Fund will cover the cost of planned local street resurfacing. Tree replacement activities have been significantly curtailed in the past years.

Operating expenditures are proposed at \$530,644, an increase of 6.68%, while capital outlay is proposed at \$575,477. The work planned for this summer is to repair Chalfonte from Fisher to Rivard. The City will also need to contribute toward the Mack Avenue resurfacing project as well.

A five year projection of future street projects, based on the continuing current level of capital expenditures, is included. It should be noted, however, that the City's 9th annual comprehensive street condition survey, conducted in accordance with state requirements, identified significantly more work that is needed, but unfunded. In recent years, major capital projects for streets have been allotted approximately a quarter of a million dollars.

This year's survey found a continuing trend of more streets that are in failed, poor and fair condition (ranked 2, 3 and 4 on a scale of 10). In order to pay for street projects, significant funding continues to be transferred from the Capital Projects fund, which will only hasten the depletion of those funds.

Given the documented need for street improvements that are evident to every driver especially after such a long hard winter, the City's road conditions will continue to deteriorate if additional funding sources are not found for this important element of the City's infrastructure. For that reason, while not assumed in the budget, City staff does recommend that a comprehensive pavement management program be funded. Given the extent of the under funding of local road for such an extended time, it will require a significant amount of new funding. Based on the engineering needs and adopting accepted principles of asset management for roads, City staff recommends a 2.5 mill increase in road funding for a period of 15 years. This amount of funding will provide what is necessary to raise the Remaining Service Life (RSL) of the roads from the current ZERO year average to above a five year RSL at the end of the 15 year program. At that point, City roads will, on average, be brought up to "good" condition. This would be accomplished by providing a mix of fixes to the City's local road program. The most cost effective use of funds for roads is to include a very strong preventative capital maintenance program, instead of just putting what little money there is toward the worst roads. The allocation of an additional millage to fund an enhanced road repair program requires approval of the residents of the City. A millage for roads could only be used for that purpose, would show as a separate item on the tax bill, and would be allocated into the Highway Fund for 2015.

PARKING FUND

The debt payments and operational costs for the Village Parking Structure are incorporated as the major cost in this budget. Occupancy in the garage has continued to increase over the past year although still less than projected before construction and the revenue generated by the structure does not cover its costs. As often has been stated, this is typically the case with public parking structures, except in major cities' urban core. However, the budget for the Parking Fund does include and has no difficulty in paying for the bonding costs for the garage entirely from parking revenues, as planned. Due to new gated parking lots in the Village, parking ticket revenue is declining (as expected and hoped) as will parking permit revenue from the loss of Beaumont Hospital permit parkers in Lot 4 when their new underground facility is completed. To improve oversight of the parking system including the new gated lots, a Parking Services Supervisor is included in this budget. A portion of the duties currently handled by the Public Service Director and other existing staff will be incorporated into this position, which will have a goal of improving customer service at its focus.

Lot 6 construction is included in the 2014-2015 budget including an electronic money collection devices to replace the parking meters, new lighting, as well as a bricked garbage enclosure designed for installation of a compactor. The next significant capital project on the horizon after Lot 6 would be Lot 4 reconstruction, which if built to the standards of Lot 2 and 3 will exceed a cost of \$1.2 million. This project likely will require bond funding to

spread out the cost of the improvement over their expected lifespan as the Parking Fund cash balance on hand will be insufficient to cover the cost.

MARINA FUND

The Marina was constructed in 2003 and is a significant asset to our community. The Marina Fund is an enterprise fund created to separately account for all marina operations. The Marina fees were increased for the 2012 boating season by 5% to address rising maintenance needs. Rates have been budgeted to remain unchanged for the 2014 boating season as the marina is returning to full or nearly full status. Marina well fees and kayak rack fees are expected to generate an estimated revenue of \$170,000, which is slightly higher than the total expenses including debt retirement. This surplus will be added to net assets for unanticipated repairs and maintenance.

DRUG FORFEITURE FUND

This federally mandated fund was established to track funds collected by the Public Safety Department from drug related property seizures and OUIL/drunk driving offenses. While these funds are not allowed to be used for officer's wages, they can be used for designated types of police equipment such as vehicles, cell phones and radios.

APPRECIATION

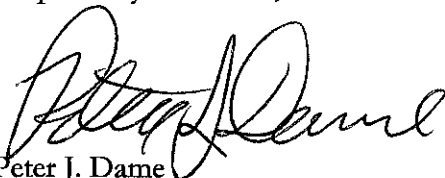
A great deal of information is contained in the following pages, and represents extensive effort by many staff members in multiple departments. Credit for this budget is given to each member of the City Staff who assisted in the process which began in January.

In particular, thank you to all the Department Directors for their participation in gathering information and for their assistance in developing the individual department budgets and flexibility in dealing with limited resources. This budget is a better tool as a result of their input.

PROCEDURE

The City Charter requires that a public hearing on the budget be held at least one week prior to its adoption. This hearing is scheduled for May 12, 2014 at 7:00 p.m. Adoption of the proposed budget is scheduled for the regular City Council meeting on May 19, 2014.

Respectfully submitted,



Peter J. Dame
City Manager



Kimberly Kleinow
Director of Finance/Treasurer