PIMA COUNTY BOARD OF SUPERVISORS
130 WEST CONGRESS, 11th FLOOR
TUCSON, ARIZONA 85701-1317

July 12, 2010

In response to the County Administrators June 24, 2010 memo regarding the Alternative Budget Proposal for Fiscal Year 2010/11 by Supervisor Ray Carroll and Supervisor Ann Day

In the beginning of our alternative budget proposal which we submitted to the Board of Supervisors on June 15, 2010, we stated that:

"The county budget is a confusing and intimidating thing for most citizens. It's a book several inches thick, filled with terms that only trained accountants use on a regular basis. Sometimes we think that the county budget is deliberately made confusing, to make it more difficult for the citizens, and even Members of the Board of Supervisors, to clearly track the expenditures."

We then proceeded to try to explain, in layman's terms, the main issues regarding the county budget: the budget surpluses, the increases in fees and taxes, and the debt of Pima County (which is more debt than all other Arizona counties combined). We also showed that our past proposal for a five percent reduction was appropriate, as even greater reductions than we advocated were implemented -- and none of the dire consequences forecast by the County Administrator ever came true.

In response to the Carroll/Day Alternative Budget proposal for Fiscal Year 2010/11, the County Administrator issued a memorandum dated June 24, 2010 which claimed to be an attempt to *"clarify the confusion and misunderstandings"* which were supposedly fostered by our analysis of the Pima County budget. Instead, this memo from Mr. Huckelberry is clearly an indication of the source of "confusion and misunderstanding."

<u>Example One: The 51.8 million General Fund Surplus</u>

The County Administrator's June 24th memo (page 3) states:

The budget General Fund "surplus" or uncommitted revenues budgeted for FY 2010/11 of about $51 million have two major components: first is $24 million for the Reserve Fund balance, which is the standard that has been budgeted for a number of years and represents approximately five percent of the General Fund. This is the minimum standard acceptable for GFOA and bond rating purposes. Another $22 million is set aside in the Tax Rate Stabilization Fund anticipating a fairly significant drop in primary assessed value of the tax base for the following year. The remaining $5 million is comprised of a number of miscellaneous reserves. This $51 million is reserved for the purpose of avoiding a significant increase in the tax rate for the primary property tax levy. It will allow the County to move strategically through the continuing contraction of the property tax base without significant tax rate shock to taxpayers or significant reductions in County services.

This directly contradicts the County Administrator's Transmittal of Recommended Budget (approved by a majority of the Board of Supervisors) which contains the following table on page 13 and clearly indicates when the General Fund Ending Balance is to be used:

Table 1
Recommended Allocation of Fiscal Year 2009/10 General Fund Ending Balance

Recommendation	Amount
Biennial Election Costs	$ 5,740,925
UPH Hospital: Additional Support	13,416,667
Non-General Fund Subsides	
• Solid Waste Services	1,500,000
• Development Services: Planning	1,500,000
• Stadium District	1,500,000
Departmental Appropriations	
• County Attorney	140,264
• Natural Resources, Parks, and Recreation	
• Pathways and Parking Lot Resurfacing Program	1,020,000
• Ball Field Lighting Replacement	1,775,000
• Playground Structures Replacement	1,175,000
General Fund Reserve at 5 Percent	24,040,215
TOTAL	$51,808,071

Nowhere in the June 24th response does Mr. Huckelberry indicate the surplus includes the extra $13.4 million for UPH/Kino, the $4.5 million for the three enterprise funds (which are supposed to be self-sustaining rather than funded with General Fund money, i.e. Primary Property taxes), nor the extra funding for the County Attorney, the Elections Division, or Natural Resources, Parks and Recreation as indicated in the adopted county budget.

On page 7 of the county budget it indicates that the $22 million for the so-called "Tax Rate Stabilization Fund" will be coming from the anticipated General Fund Surplus for Pima County for the coming fiscal year:

- It is recommended that the $22,354,490 of excess General Fund revenues be set aside in the Property Tax Stabilization Fund in order to avoid precipitous future property tax increases that would otherwise be necessary to address projected deficits for the next several years, including a $24,584,378 loss in Fiscal Year 2011/12 resulting from a projected 8.3 percent reduction in the value of the primary property tax base.

There is likewise, no clarity in the Administrators latest memo in his reference to the *"remaining $5 million for "miscellaneous reserves."*

The Administrator's summarized distribution of General Fund surplus and his data provided in the adopted county budge,t versus his June 24th memo, only adds to the noted "confusion and misunderstandings."

Example 2: The Effect of a 10% Reduction

As noted in the Carroll/Day alternative budget statement, when we proposed a five percent reduction two years ago we were informed by the Administrator's office that our proposal would cause:

"the layoff of as many as 260 County employees, including 156 law enforcement personnel; reductions in essential court services ... elimination of security services at County buildings; closure of some parks and swimming pools; 6000 fewer animal enforcement responses per year; elimination of remote early voting sites; elimination of bus routes; etc." [From the April 7, 2008 memo from Thomas House, Budget Manager]

We pointed out that there actually was a 10 percent reduction (rather than our 5 percent proposal) in that time period and there were no layoffs – but rather a $51.8 million surplus. For this reason, we thought it was appropriate to propose a 10% reduction this year to provide some tax relief for our citizens. In response, the Administrators memo states that such a reduction of 10 percent would ***"require the Sheriff to lay off 50 sworn law enforcement offices, reduce the number of correction officers by 45, and take other actions that are clearly inappropriate..."***

So, our proposal to cut the budget by 5% two years ago would have caused the layoff of 260 employees, but our current proposal to cut 10% would only cause the layoff of 50?

On top of that, the Administrator's memo states that there have been ***"well thought out budget reductions in the last three years totaling 10 percent."*** Yet the adopted budget states [page 16] that ***"The cumulative reduction in department budgets during the past two years has been approximately 10 percent."*** {Emphasis ours]

Does a ten percent reduction amount to 50 layoffs, 260 layoffs, or no layoffs? Has there been a 10 percent reduction for two years, or that reduction over three years?

The source of confusion is clearly not with any member of the Board of Supervisors, but with County Administration.

Pay-As-You-Go versus Increased Debt

The issue of "Pay-As-You-Go," or to spend money that we have available (and live within our means) rather than to go further into debt, was an option first proposed by Supervisor Sharon Bronson a number of years ago which was, unfortunately, ignored. Although this was not a formal proposal as contained in the Carroll/Day budget proposal, it is an idea that was raised by Supervisor Carroll in his recent analysis of ever growing Pima County debt, in which he suggested it ***"rather than forcing future generations with the burden of long-term debt, we should adopt a Pay-As-You-Go system, at least until some of our debt is paid down."*** He stated it should be considered as ***"one solution to long term debt."***

The County Administrator has unilaterally rejected the Pay-As-You-Go system, claiming in his June 24th memo that:

"...paying for our ADEQ-imposed wastewater treatment plant upgrades with pay-as-you-go financing would require a rate increase of 136 percent, something that would be detrimental to the rate payers of Pima County."

Yet it is likely that this is what will happen with the Administrators plan – which includes an additional $700 million for Wastewater bond debt, necessitating an increase in our sewer fees to such a level or higher. We have already seen an increase in fees up by 43% percent. If we go into further debt, there is only one source to pay back that debt, and that is ever increasing sewer user fees for the foreseeable future. Increasing sewer fees are just another added form of increased taxation. We agree that such astronomical increases are *"detrimental to the rate payers of Pima County."* Why then is the Administrator proposing them?

<u>Well Managed Debt?</u>

Mr. Huckelberry claims on page 4 of his memo that Pima County's debt is *"well managed."* He made a similar claim in a Tucson Weekly article in which he said that it is not the size of the debt that matters, only how it is managed. We do not agree – we believe the size of the debt matters very much, and should matter to current taxpayers and how such debt will affect future generations. Be that as it may, how well is our debt really managed?

Let us look at three main types of debt in which Pima County is currently responsible:

<u>The 1997 HURF Funds</u> are certainly not well managed. Pima County has not delivered what was promised to the taxpayers. One prime reason for this is the size (and management) of the debt. As indicated in a recent Arizona Daily Star story (included in our alternative budget proposal), the Director of our Transportation Department indicated that there is still $100 million in unsold road bonds – bonding for projects which were supposed to have already been used several years ago. The reason that these bonds cannot be sold today is because existing HURF revenues are only sufficient to cover the debt. Does this indicate a well managed debt?

<u>The G.O. Bonds</u> are paid by secondary property taxes, which are going up this year based on the budget adopted by the Board majority. Debt service is paid by these property taxes, and the more debt we incur the more burden is created on the back of the taxpayers. When property valuations go down – which they will next year – the only way available to pay the debt service – which *must* be paid -- is to raise the rates of the secondary taxes. Are ever increases taxes to pay off every increasing debt an indication of a well managed system of debt?

Finally, there are COP's or <u>Certificates of Participation</u> – non voter approved debt in which publically owned county facilities are used as collateral. The majority of this debt is paid out of the General Fund, that is, Primary Property taxes. For years, Pima County did not utilize this form of debt for obvious reasons, but in the last few years COPs have put us hundreds of millions more into debt. Does this sound like good management?

Most of us sitting in positions of responsibility in Pima County will probably not be here in 30 years, but our legacy will be felt by our children and grandchildren. They will look and wonder, as some are doing today, how their "leaders" could have got us into such a financial mess. Maybe some will say we were just "confused." Ultimately, there are no excuses. The time is quickly running out for Pima County to change course and to act with fiscal restraint and with some social responsibility. In August we will set the tax rates, and we still have a chance to reduce them and offset some of the burden being placed on our constituents. We hope the Board majority will consider these issues seriously, as we will continue to offer alternatives to the county's ever growing and costly bureaucracy.

Respectfully submitted,

Supervisor Ray Carroll
District 4

Ann Day

Supervisor Ann Day
District 1

MEMORANDUM

Date: June 24, 2010

To: The Honorable Chairman and Members
Pima County Board of Supervisors

From: C.H. Huckelberry
County Administrator

Re: **Fiscal Year 2010/11 Budget Statement of the Honorable Supervisors Ray Carroll and Ann Day Submitted to the Clerk for Inclusion in the Public Record on June 15, 2010**

This is to clarify the confusion and misunderstandings contained in the budget statement prepared by Supervisors Carroll and Day, which was distributed to the Board at Final Budget Adoption and has since been posted on the internet for public information and review.

The County Does Not Have a Huge Budget Surplus

Regarding the calculation of and conclusions about the budget surplus, it is important to understand that the schedules or summaries that were distributed with the Budget materials are in a format required by law and established by the State Office of the Auditor General. While the Budget is the manifestation of public policy set by the Board, the Budget is ultimately an accounting instrument that must be set out pursuant to uniform standards that can be universally reviewed within that fiscal discipline. It is easy to see how Supervisors Carroll and Day misinterpreted and misunderstood the prescribed budget forms and mistakenly concluded the County had a "huge" budget surplus of $487 million.

Using the Auditor General's schedules, the budget "surplus" can be misunderstood because the proceeds of sewer obligation debt sales restricted to wastewater capital improvement projects in the amount of approximately $300 million are included as available resources, but expenditure of these dollars is not. In budgeting for this enterprise fund, accounting principles dictate that revenues are budgeted and capital expenditures are not (although they are footnoted and reported elsewhere in the budget document), even though the $300 million in sewer revenue obligations will be spent for capital improvements required by the Arizona Department of Environmental Quality (ADEQ). In addition, the capital projects surplus references bond funds in advance of expenditures; therefore, the surplus is to be used to pay actual expenses of the capital improvement program prior to the next bond sale.

Further confusion is raised in the commingled discussion of balances in special revenue funds. The special revenue funds include the Transportation Department, Regional Flood Control District and Library District, all of which are funds restricted by State statute. Intermingling these funds or using them to reduce primary taxes would be illegal.

Because of the standard forms required by the Auditor General, it could be misconstrued that we have a very large General Fund balance. We do not. The budgeted year end General Fund balance for Fiscal Year (FY) 2010/11 is barely acceptable pursuant to accepted principles of the Government Finance Officers Association:

"The Government Finance Officers Association (GFOA) recommends that governments establish a formal policy on the level of unrestricted fund balance that should be maintained in the general fund. Such a guideline should be set by the appropriate policy body and should provide both a temporal framework and specific plans for increasing or decreasing the level of unrestricted fund balance, if it is inconsistent with that policy.

Nevertheless, GFOA recommends, at a minimum, that general-purpose governments, regardless of size, maintain unrestricted fund balance in their general fund of no less than two months of regular general fund operating revenues or regular general fund operating expenditures."

http://www.gfoa.org/downloads/AppropriateLevelUnrestrictedFundBalanceGeneralFund_BestPractice.pdf

"In preparing the original 2002 best practice, the GFOA intended to set a minimum target of approximately two months of operating revenues or expenditures, while at the same time acknowledging that an amount as low as 5 percent could be appropriate for very large governments. Accordingly, the original best practice spoke of a minimum target of "no less than 5 to 15 percent."

http://www.thefreelibrary.com/GFOA+updates+best+practice+on+fund+balance.-a0214711169

The actual FY 2009/10 fund balance in each of our tax funds is shown in the table below and equals approximately 17 percent of gross revenue. The GFOA sets a minimum standard that "no less than two months of operating revenues" be maintained as a General Fund balance. Two months of the 12 months for the General Fund equals 17 percent; yet our General Fund balance is only at 11 percent. The fund balance is on target based on nationally accepted, conservative finance and management best practices. Even the combination of all funds derived from property taxes is only at 17 percent.

Special Revenue Fund Balances

Description	Fund Balance	FY 2010 Revenue
General Fund	$ 51,808,071	$488,552,225
Library District	13,023,146	28,200,402
Flood Control District	7,105,277	23,598,588
Debt Service	38,689,263	111,052,462
Total	$110,625,757	$651,403,677

Why These Fund Balances are Good Fiscal Policy

The budget General Fund "surplus" or uncommitted revenues budgeted for FY 2010/11 of about $51 million have two major components: first is $24 million for the Reserve Fund balance, which is the standard that has been budgeted for a number of years and represents approximately five percent of the General Fund. This is the minimum standard acceptable for GFOA and bond rating purposes. Another $22 million is set aside in the Tax Rate Stabilization Fund anticipating a fairly significant drop in primary assessed value of the tax base for the following year. The remaining $5 million is comprised of a number of miscellaneous reserves. This $51 million is reserved for the purpose of avoiding a significant increase in the tax rate for the primary property tax levy. It will allow the County to move strategically through the continuing contraction of the property tax base without significant tax rate shock to taxpayers or significant reductions in County services.

The Library District fund balance of $13 million is also part of a tactical management and budget plan associated with transition of the library system to the County. The fund balance was increased to accommodate unanticipated costs in the transition. The transition has occurred without major issues. This year, the fund balance in the Library District is being reduced nearly $5 million to offset the required increase in the tax rate that would otherwise be needed to fully fund library operations. The budget policy for the Library District is to gradually increase the tax rate so that it can sustain the library system budget in the long term. This fund balance will be further reduced next year as the secondary assessed value continues to contract.

The Regional Flood Control District fund balance of $7 million is appropriate given the unpredictability in budgeting required capital contributions to federally funded flood control projects through the US Army Corps of Engineers. Many of these projects are funded on a Congressional appropriations basis, and it is unknown from year to year when major federal appropriations will be received; hence the need to maintain a relatively high fund balance to match federal funds should they be appropriated by Congress.

Finally, the Debt Service fund balance of about $39 million consists of $3.7 million for General Obligation debt service and $35.3 million transferred from Regional Wastewater Reclamation to pay for one-time "bridge" financing from the 2008 and 2009 Series Certificates of Participation. These reserves are appropriate to ensure we continue to have the ability to manage our debt with short repayment periods and level debt service such that we do not backload debt payments or extend the life of bonds from the short 15-year period we have always advanced for debt management.

Why These Fund Balances are Important

The Tax Rate Stabilization Fund is of particular importance given the economic forecast associated with the declining Pima County property tax base. On January 20, 2010, I transmitted to the Board an updated economic forecast of the tax base; this update superseded the forecast provided to the Board on April 28, 2009. In my memorandum of January 20, 2010, the primary tax base decreased by 0.51 percent for FY 2010/11 and was forecasted to decline by another 8.2 percent for FY 2011/12. This is a record decline in the primary property tax base since the advent of the present property tax base system in Arizona dating from the 1960s.

In addition, secondary assessed values decreased by 5 percent in FY 2010/11 and are forecasted to decrease another 10.8 percent for FY 2011/12. These forecasted declining property tax bases require budget planning and management preparation; hence the recommendation to the Board to set aside significant reserves in the Tax Rate Stabilization Fund.

Proposal to Use the Fund Balance to Reduce Taxes

The General Fund balance for FY 2009/10 could be used to reduce property taxes; however, such would set the County up for fiscal calamity, since our fund balance would be exhausted, our bond ratings would be downgraded and the set aside to cushion the forecasted and real decrease in assessed values next year would be squandered. The result would be a rollercoaster of precipitous instability for both commercial and individual taxpayers that would not facilitate responsible fiscal policy.

The establishment of fund balances and surpluses is a deliberate, conservative exercise of strategic planning to reduce the adverse effects of the declining economy, both to eliminate rate shock for taxpayers who would bear the burden of a yo-yoing tax rate, as well as those who rely on the essential services of the County for their well-being during this economic mega-recession.

The Assertion that the County is Drowning in Debt and Plans to Dive Much Deeper into Debt

Our debt is well managed and more fiscally conservative than most local governments that issue debt. As an alternative to our current use of short-term debt financing, we could employ a pay-as-you-go strategy. Paying for our ADEQ-imposed wastewater treatment plant upgrades with pay-as-you-go financing would require a rate increase of 136 percent, something that would be detrimental to the rate payers of Pima County. While one could state we were using pay-as-you-go financing, it would be of little consolation to those who could not afford such a payment. The same is true for our voter authorized General Obligation debt. The Board could levy a sufficient secondary tax rate to pay off this debt or any other existing debt from previous authorizations; however, it would require a tax rate increase of $0.8501 just for FY 2010/11 projects and an additional increase of $5.5663 to pay existing outstanding debt.

I believe the voters clearly understood the benefit associated with the issuance of bonds. Since most have a mortgage on their homes, they understand the concept and principle of debt financing. I believe it is also understood that the life of most of these capital improvements – 50 years or more – will span and benefit many different property owners as residents and businesses come and go from our County over the decades, and these capital costs should be apportioned accordingly. The voters overwhelmingly approved debt financing for a series of public improvements we are now implementing and paying off; and by any traditional governmental standard, paying off at substantially accelerated rates.

<u>Tax Relief or Pay Off Debt?</u>

The Carroll/Day budget statement that "in fact, tax increases are proposed" requires, I believe, some scale and context. The total Pima County primary tax levy for this year is $296,197,333; last year it was $297,723,590. The difference is a tax decrease. The total levy for all secondaries is $125,272,219 this year versus $123,491,571 last year: essentially flat. Adding the two together, this so called tax increase, spread over the population of the County, is 25 cents per year per capita, despite substantially decreasing state shared revenues and cost shifts.

The budget statement of Supervisors Carroll and Day fails to recognize that the County tax base is contracting; the County economic forecast of which Supervisors Carroll and Day are aware indicates the tax base will continue to shrink for the next three years. I continue to believe it is prudent to establish a secondary rainy day fund to reduce the likelihood of future tax increases. Given the delicate state of the local economy, this Property Tax Stabilization Fund is designed specifically to avoid unpredictable future tax increases.

<u>The Budget Proposal of Supervisors Day and Carroll Requesting a 10 Percent Cut</u>

To reduce General Fund expenditures across the board by 10 percent would require the Pima County Sheriff to implement an $11.8 million reduction in expenditures. This would require the Sheriff to lay off 50 sworn law enforcement officers, reduce the number of corrections officers at the Adult Detention Facility by 45, and take other actions that are clearly inappropriate and inconsistent with the Board's goal to maintain public safety standards at the highest possible level.

County departments and agencies have undergone planned, well thought out budget reductions in the last three years totaling 10 percent. It is likely future measured reductions will be required. To request or require an additional 10 percent reduction is an arbitrary and unnecessary burden at this time.

If you have any questions or require additional information regarding this analysis, please contact me.

CHH/mjk

Attachment

c: The Honorable Jan Kearney, Superior Court Presiding Judge
Elected Officials
Appointing Authorities