



# MEMORANDUM

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**DATE:** December 3, 2008

**TO:** The Honorable Mayor and  
Council Members

**FROM:** Mike Hein  
City Manager

**SUBJECT:** Fiscal Year 2009 Budget and Look at Fiscal Year 2010 – December Update

The structure of local government has permanently altered. The most recent revenue projections represent levels equal to or less than those in the adopted in FY 2005 budget. Tough decisions must be made to prioritize diminishing resources.

The City of Tucson has been fortunate compared to many of its peers. We have been able to avoid drastic reductions in public safety and wide scale layoffs because of the basic stability of the local economy anchored by Davis Monthan, University of Arizona, and other typically less recession vulnerable institutions coupled with the foresight of the Mayor and Council through its embracing of the financial sustainability plan and having growth in revenues pay for growth in services.

The End of Service program has provided an avenue for us to strategically cut and redeploy our human capital. The City has slowly been able to control expenses and employ one time, non-recurring fiscal practices to assist with covering deficits for this fiscal year. All of these measures have not been enough to keep up with the escalating fall in our local and State shared sales tax. This year will require strategic re-tooling of how we approach business as local government.

In September and October, the City's financial status was illustrated for you in a table identifying budget demands versus budget management measures. The table format has proved useful in evaluating our current adopted budget against projected revenues. However, the table does not give us a clear indication of how our current and projected expenditures are trending against revenues. (Note: Appendix A)

Due to the unprecedented shortfall in revenues, the FY 2009 adopted budget is now significantly lower than what was approved. Our most recent projections now place the shortfall at \$44.7 million. Budget management measures have addressed \$13.6 million of the shortfall resulting in an additional \$31.14 million in cuts. To continue to show revenue and expenditure projections as variances against that budget does not illustrate where we are today. In future communications with the Mayor and Council, the Finance Department will be presenting the status of the General Purpose Funds as a variance between total projected revenues and total projected expenditures.

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This format will focus on what we know today, not what we thought would happen when the budget was adopted. The projection of real time expenses will give us a better financial forecast to compare with our projected expenditures.

Given that the economy has not experienced the magnitude of the current recession in many decades, no one can give a definitive, educated estimate for future revenues. In addition to the format change on tracking our deficit, the Finance Department has incorporated these changes into two scenarios for revenue projections. The scenarios present a probable and a potentially worst case projection for how the City's budget may fare this year. The scenarios will be updated monthly. While this methodology does not provide *crystal ball* accuracy for how we will end the year, it will allow us to track and project our deficit based on current revenue and expenditure trends. This is important considering the continuing decline shown in October revenue collections.

**Projected General Purpose Fund  
Fiscal Year 2008/2009  
As of December 1, 2008**

	Scenario I	Scenario II
Projected Revenues	448,742,591	444,648,395
Reduced Administrative Services Charge to DSD	(2,300,000)	(2,300,000)
Plus Rio Nuevo Loan Receipts	6,800,000	6,800,000
Total Projected Revenues	453,242,591	449,148,395
Less Projected Expenditures	(505,908,282)	(505,908,282)
Plus Restructuring of July 1, 2009 Debt Service	10,000,000	10,000,000
Transfer to State	(2,100,000)	(2,100,000)
Total Projected Expenditures	(498,008,282)	(498,008,282)
Excess Expenditures Over Revenues	(44,765,691)	(48,859,887)

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As of November, revenue trends continue to indicate that we have not seen the bottom of our revenue declines. As illustrated in the chart below, November sales tax receipts are down 8.06% locally and 7.28 % at the State level.

<b>Monthly Analysis of City Sales Tax Revenues (\$ millions)</b>						
	<b>FY 2008</b>		<b>FY 2009</b>		<b>YTD Decrease</b>	
	Month	YTD	Month	YTD	\$ Drop	% Drop
<b>July</b>	16.5	16.5	15.5	15.5	-\$0.9	-5.74%
<b>August</b>	16.5	32.9	15.2	30.7	-\$2.1	-6.67%
<b>September</b>	16.2	49.1	15.2	46.0	-\$3.1	-6.39%
<b>October</b>	16.0	65.1	14.2	60.2	-\$4.9	-7.53%
<b>November</b>	15.9	81.0	14.2	74.4	-\$6.5	-8.06%

  

<b>Monthly Analysis of State-Shared Sales Tax Revenues (\$ millions)</b>						
	<b>FY 2008</b>		<b>FY 2009</b>		<b>YTD Decrease</b>	
	Month	YTD	Month	YTD	\$ Drop	% Drop
<b>July</b>	4.2	4.2	4.0	4.0	-\$0.2	-4.19%
<b>August</b>	4.2	8.4	3.8	7.8	-\$0.6	-7.01%
<b>September</b>	4.0	12.4	3.7	11.5	-\$0.9	-7.23%
<b>October</b>	4.0	16.3	3.7	15.2	-\$1.2	-6.87%
<b>November</b>	4.0	20.3	3.6	18.8	-\$1.5	-7.28%

### ADDRESSING THE DEFICIT FOR FISCAL YEAR 2009

**What have we already done to cut costs?** The attached (Note: Appendix B) report from Assistant City Manager Richard Miranda provides a blueprint for the Mayor and Council on core services that departments deliver and the \$13.3 million in cuts approved in September and the impact of those cuts on departments. To accomplish these savings 162 positions were eliminated, departments' operating costs were reduced and reductions in Outside Agencies contributions were implemented.

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In the October 16, 2008 memorandum to Mayor and Council, *Fiscal Year 2008 and 2009 Budget- October Update*, we indicated that \$13.6 million in additional cuts had to be made as part of our budget management measures. The attached (Note: Appendix C) following budget management measures have been implemented to address the \$13.6 million shortfall.

**What budget management measures must be implemented now to address the revenue shortfall?** The \$31.14 million (scenario 1) budget management measures are indicated in the chart.

**General Purpose Funds Budget Cuts  
Fiscal Year 2009  
PHASE TWO  
Pending Mayor & Council Approval**

Settlement of W. Grace lawsuit	(5,300,000)
Use of Fund Balance	(5,000,000)
Reduction of Transit Subsidy to \$36 million	(3,000,000)
Delay Public Safety Academies	(4,000,000)
City Court revenue increase	(2,500,000)
Defer payment to State	(2,100,000)
Operating Transfer from Vehicle Replacement Fund	(1,000,000)
Parks Leisure classes, TCC, Golf	(1,000,000)
Increase Recovery from Impound Fees	(400,000)
Back 2 Basics (unallocated to projects)	(160,000)
<b>Total of Phase II Budget Reductions</b>	<b>(24,460,000)</b>
<b>Management Expenditure Reduction Plan</b>	<b>(6,678,838)</b>
	<b>(31,138,838)</b>

A number of the budget management measures totaling \$34.2 million are not recurring savings and will need to be addressed by reductions or revenue enhancements in Fiscal Year 2010.

**NON- RECURRING**

Debt Restructuring	(10,000,000)
Delay of Academy	(4,000,000)
Settlement of W. Grace lawsuit	(5,300,000)
Use of Fund Balance	(5,000,000)
Payment to State	(2,100,000)
Operating Transfer from Vehicle Replacement Fund	(1,000,000)
Rio Nuevo Loan Repayment	(6,800,000)
	<b>(34,200,000)</b>

No one is predicting with any certainty when this current recession will end. The City will be prepared for the worst and is planning for it. In looking beyond FY 2010, we must continue to

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protect our reserves and explore all avenues for addressing the impact that service cuts will have on our citizens. Additionally, we have to look at further cuts or new revenues that will cover the loss of the \$34.2 million in one-time savings, which include the repayment of the Rio Nuevo Loan (\$6.8 million) and the bond restructuring (\$10 million). The City could continue to buy time by further debt restructuring in FY 2011, but this will result in higher debt costs in the future. It is important to realize that these two measures are a short-term fix that will have to be replaced by permanent cuts or revenue solutions in the future.

## **CASH MANAGEMENT**

In addition to budget management measures, we will also have to improve our cash management practices. The City has never had a comprehensive cash management strategy. In the past there was no urgency to develop a strategy since financing received from voter-approved bonds and certificates of participation (COPs) provided short-term cash for the city to use in months when revenues were not keeping up with expenditures.

This cash float was available until the capital projects were underway. Recently, funds have also been provided to capital projects after authorization for borrowing, but before funds from the borrowing were received, which has reduced our cash availability. The Interim Finance Director is recommending the establishment of a line of credit to address the City's cash management situation. The line of credit will only be used when cash on hand is less than necessary for our bills that have to be paid. The line of credit will have to be fully repaid by the end of the fiscal year.

## **A LOOK AT FISCAL YEAR 2010**

The General Purpose Revenues for FY 2010 are projected at \$431.7 million. This projection could result in revenue shortfalls of over \$70 million. The reductions made by the City in FY 2009 will continue to pay dividends in FY 2010. Please note further detail in (Note: Appendix C).

One major uncertainty in projecting Fiscal Year 2010 is how the State will balance its current and future deficits. Our current projections for FY 2010 are based on current and expected trends for the State-shared revenues deposited in the General Fund. The City will also need to address potential deficits that might occur due to reductions in State-shared Highway User Revenue Fund (HURF) revenues.

### **Highway User Revenue Fund (HURF)**

HURF is used to fund streets, drainage and right of way maintenance. Back to Basic projects are also partially funded out of HURF. Funding for HURF comes from revenues that the State receives from licenses, taxes, penalties, driver's licenses and fuel taxes. For decades, the City has used debt financing for HURF-related projects. The combination of repayment of this debt,

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operating costs and reduced revenues will result in a projected deficit of approximately \$3 million in FY2009.

To address this HURF deficit, all current and future vacancies in Transportation will be cut, debt will be restructured and measures will be taken to reduce operating costs. If the deficit in the HURF fund is not managed, it will eventually impact the General Fund reserves.

## RECOMMENDATIONS

The current financial times require both immediate and long-term measures and strategies for addressing the deficit. The recommendations below provide immediate action and more long term policy decisions for the Mayor and Council's consideration at a future Mayor and Council meeting in early 2009. Staff will submit a FY 2010 budget calendar for your approval at the Tuesday, December 16<sup>th</sup> Mayor and Council meeting.

Mayor and Council are requested to direct staff to proceed on the following:

- Implement the \$31.14 million in additional budget management measures.
- Submit the necessary documentation to authorize a letter of credit.
- Submit the necessary documentation for a two-year refunding of HURF debt.

Mayor and Council are requested to provide future policy direction on the following:

- Recommended level of outside agency support.
- Addressing the General Fund subsidies to Tucson City Golf, Tucson Convention Center and Sun Tran/Van Tran.
- Exempt Golf, Tucson Convention Center, City Clerk's Office and Parks from non-permanent hour restrictions under City Ordinance and part-time employee benefit eligibility.
- Investigating full-cost recovery for city services.
- Explore changing benefits for new employees.
- Returning to the General Fund any savings from the low-income subsidy for the utility programs, rather than to the Housing Trust Fund.
- Eliminating all classes and programs in the Parks and Recreation Department that are provided privately or by other governments.
- Work with the Labor Council on implementing any reductions related to contracts or working conditions for covered employees.
- A review of the mission and goals for each department to determine what the core service delivery should be for services provided by the City of Tucson.
- Elimination of departments, divisions and programs i.e. Urban Planning, Channel 12 and Neighborhood Outreach.
- Aggressive annexation of revenue producing areas.
- Maximizing Grants and other Federal Funding.
- Potential closure and consolidation of fire stations and other public facilities.
- Eliminate Public Access Funding.

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- Reduce funding for Metropolitan Tucson Convention and Visitors Bureau over five years to statutory requirement.
- Consolidation of departments.
- Eliminate Funding to School Plus Jobs.
- A review of medical benefits and other employee benefits.
- Increasing fees and fines for both civil and criminal offenses.
- Development of processes that provide evaluation and examination of the effectiveness of outside agencies who receive funding from the City of Tucson.
- A review of our capital planning so as to reduce our debt service obligations.
- Increases in fees for use of City of Tucson facilities such as the public safety Training Center, recreation facilities and services provided for special events to ensure full cost recovery for our services.
- Update cost allocation charges to Environmental Services and Water for General Fund support.
- Sale of surplus property.

The discussion and direction provided by Mayor and Council on these policy issues will set the stage for staff to prepare the FY 2010 budget. A memorandum delineating the cost savings or potential revenues from these policies will be sent to you in January.

In all likelihood, if all of these policy measures were pursued they may not be significant enough to address our \$34.2 million in non-recurring revenues and further shortfalls in revenues in FY 2010.

A number of additional issues have been addressed or are at the point of examination. Issues such as take home vehicles, cell phones, travel and on call pay have been thoroughly examined and it is felt that we are working efficiently as possible in these areas to keep costs down without impacting services. Examination of ideas such as the selling of assets, the selling of property, coordination of economies of scale with other government entities and employee furloughs is currently on going in our contingency planning.

## **FEEDBACK AND INPUT ON BUDGET MANGEMENT MEASURES**

The ever changing financial landscape for the city will require communication and feedback on the direction we are going with the budget management measures and ideas for further reductions or revenue enhancements. Information on our budget has been and will continue to be posted on the City of Tucson Internet and Employee Intranet web page. Many departments have discussed our budget challenges with their employees. We expect for Mayor and Council to continue to offer Town Halls for communicating with our citizens. A new website will be offered to employees for them to submit suggestions on addressing our financial challenge.

If you have any questions regarding this memorandum, please do not hesitate to contact me.