

Ensuring Fiscal Health (Part One – February 09 issue)

The collapse of the national housing market, the credit crunch and the subsequent slowdown in the economy in recent months is having and will have an impact on state and local government budgets. The economic downturn recently caused the State of Iowa to cut spending across-the-board 1.5 percent for FY2009 and early budget estimates for FY2010 are not optimistic as anticipated expenses meet declining revenues.

The 1.5 percent across-the-board reduction at the state level for the current fiscal year is estimated to save the state \$91.4 million. These cuts include about \$1.2 million for programs of particular interest to local government including reductions to the Community Development Block Grant Program, Iowa Power Fund and the Property Tax Credit Fund. State cuts for the current fiscal year are largely manageable for local governments. The big unknown is the level of reductions that will be needed for the state to balance its budget for FY2010.

The same national economic trends impacting state government revenues will also influence local government budgets over the course of the next several budget cycles. The extent of this influence will largely depend on the health of your local housing market and the supply (and diversification) of sales tax generating businesses in and around your community. Iowa by most indications is better off than national averages, but it is still an appropriate time to prepare for tough budget times. This article is intended to provide general suggestions and advice on issues related to coping with reduced resources both in the short term and the long term.

Take a deep breath

While we are entering a period of instability, it is still important not to panic. It is crucial that decision making be strategic, measured, consistent with citizen priorities and sensitive to the concern of employees. Cities should examine all options, work closely with employees and the public, and make the choices that are best for the community. There are certainly some principles that city officials will want to keep in mind. Most important is the need for a long term strategy. As a practical matter, this implies services may need to be reduced if permanent savings are going to be realized. Short term solutions may be more popular, and may be appropriate to help make ends meet until other solutions are found.

If service reductions involve reduced maintenance standards or response times, it is likely that this should be formalized in some fashion. Consultation with the city attorney is imperative to determine the form and the substance of a policy decision of this nature.

City officials need to monitor the results of decisions made and make modifications as necessary. No one can fully anticipate the potential impact of such decisions, and even if that were possible, circumstances change. The service that seems optional today may be indispensable tomorrow. Citizen attitudes might also change.

Expenditures

As revenues decline, cities typically examine where they can reduce costs or eliminate expenditures. Cities may consider across-the-board reductions or may choose to examine specific expenditures within the budget. While across-the-board cuts seem equitable, they may not appropriately consider long-term projects that can be negatively impacted. Not all city programs and spending enjoy the same level of use, need and support. It is hard to treat fireworks for a 4th of July celebration and clean drinking water in the same manner. Prioritization of spending is a difficult but necessary step elected officials must take during tough budget times.

In the short term, the city may propose delaying or altering a major project. For instance, the city may be considering a water park to replace an aging swimming pool. The city may defer the water park until alternate funding can be found or alter the project to something less costly. In the long term, cities may decide to re-evaluate their capital improvement plans to prioritize and fund those major improvements deemed most necessary.

Cities can delay purchasing items, such as office equipment or vehicles, and attempt to extend the life of equipment or supplies, or lengthen the replacement cycle for vehicles. Such an approach must be taken carefully to avoid increased maintenance costs offsetting any potential savings. For the long term, cities should consider group purchasing options to maximize cost savings. Group purchasing programs, such as U.S. Communities located at www.uscommunities.org, allow cities to take advantage of discounts given to large entities. Cities can take advantage of State of Iowa contracts equipment, for more information visit www.iowadot.gov/purchasing/ or

<http://das.gse.iowa.gov/procurement/>. Cities can also join with other political subdivisions, such as counties and schools, to identify commodities that can be purchased as a group.

Working with independent boards

Certain city departments enjoy a greater degree of financial autonomy, either by virtue of state law or by the nature of their operations. For example, utility boards typically have oversight of their operations. Library boards and parks and recreation boards may enjoy a significant degree of oversight of their budget and revenues. The degree of independence a board enjoys may be outlined in the city's ordinance. In certain cases, the city council may need to make reductions in the budgets that are overseen by an autonomous board. Communications between the city council, the board and their staffs will be the key to successfully addressing the required spending reductions. Both need to remember that the budget is only an appropriation. It is not a guarantee of income. Both the city and the boards will need to work together in amending priorities and determining adjusted spending levels.

Personnel Changes

For most cities, personnel costs represent a high percentage of their general fund expenditures, in both wages and benefits. It is only logical that cities may look to staff reductions in order to reduce costs. Layoffs, hiring freezes and organizational restructuring are all options. Each of these, however, has potential costs and long term impacts, both on the city's budget, the efficiency of the organization and staff morale. Reductions in staff can be fairly expensive as a city needs to consider unemployment costs, unused vacation payouts and compensatory time liabilities. For these reasons, cities need to clearly understand their objectives, carefully consider their options and act prudently. Cities can also evaluate their benefits to determine if health insurance deductibles, employee contributions and rates are in line with market averages. As with most personnel issues, cities must consult with their city attorney to ensure they are protecting the rights of their employees and mitigating any potential liability.

Revenues

Regardless of your revenue sources, it is important to review your assumptions for how your city estimates revenues. How will those sources be impacted by national economic trends? Will funding be impacted by further state budget cuts?

The most common form of revenue for the city is the property tax. It is a 2009 legislative priority of the Iowa League of Cities, as well as a recommendation of the Legislative Property Tax Study Committee, to diversify revenues sources in hopes of reducing the reliance on property tax. While we hope to report success in obtaining alternative revenues for cities during the legislative session, there are several other options to the property tax that city officials can consider right now.

Many city services are supported through fees. Fees can be collected on licenses for animals or businesses, permits for housing or contractors, and entrance to recreational facilities such as a swimming pool. Services currently supported by the general fund can sometimes be converted to enterprises, such as garbage collection. Several cities have also started a storm water sewer utility. Fees may be more acceptable to citizens because a direct connection is drawn from the fee paid to the service provided. The amount of the fee should be enough to cover all the expenses of the service provided. Revenue generated beyond this could be challenged as an illegal tax. Surcharges added to existing utilities should be avoided as these can also be challenged as an illegal tax.

Another opportunity for supplementing revenue is through fines. Fines are intended to not only dictate behavior, such as obeying traffic laws, but also provide revenues to cover enforcement. Enacting traffic laws as city ordinance ensures the majority of the fine is refunded to the city. This is not the case if the traffic infraction is written under state law. Cities should also review their municipal infraction ordinance, or consider adopting such an ordinance. Any changes to fines or enforcement methods should be reviewed with the city attorney.

Conclusion

Reducing services or increasing revenues are not popular choices, but they are solutions to keep the fiscal health of the community intact during tough budget times. City officials will want to maximize public participation to ensure service cuts or revenue increases are accepted by the community at large. Such participation can deepen public understanding and begin building better community support for city services. City officials did not ask for this challenge, but it is up to us to face it. It will require that we use all the skills and assets in our communities.

Questions about this article may be directed to the League at mailbox@iowaleague.org.

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Strategies for fiscal health a long-term perspective (part two – March issue)

By Jeff Schott

As cities cope with the challenges of our current tough economic conditions, considerable attention is focused on immediate, short-term budgetary issues. The article “Ensuring Fiscal Health” in the February issue of Cityscape (pages 14-15), discussed several helpful short-term approaches in dealing with these issues.

But it is equally important that cities maintain a long-term outlook on their financial situation. The purpose of this article is to suggest several strategies by which cities can promote their long-term fiscal health.

Strategic Budgeting

Especially in periods of limited financial resources, policy makers should adopt a strategic approach to budgeting. Establishing priorities and developing benchmarks can provide direction to policymakers and help local governments stay on course.

The National Advisory Council on State and Local Budgeting (NACSLB) recommends a goal-oriented approach to budgeting based on the following framework:

Principle I – Establish broad goals to guide government decision-making:

- Assess community needs, priorities, challenges and opportunities.
- Identify opportunities and challenges for government services, capital assets and management.
- Develop and disseminate broad goals.

Principle II – Develop approaches to achieve goals:

- Adopt financial policies.
- Develop programmatic, operating and capital policies and plans.
- Develop programs and services that are consistent with policies and plans.
- Develop management strategies.

Principle III – Develop a budget with approaches to achieve goals:

- Develop a process for preparing and adopting a budget.
- Develop and evaluate financial options.
- Make choices necessary to adopt a budget.

Principle IV - Evaluate performance and make adjustments:

- Monitor, measure and evaluate performance.
- Make adjustments as needed.

Reconciling Short- and Long-Range Planning

Recognize the longer-term financial impacts of short-term budget decisions. Capital projects, debt financing of such projects, and many annual budget decisions affect budgets far into the future. Identify the projected operating and/or personnel costs associated with providing current and anticipated services, projects and programs (adjusted for inflation) before committing to the initial funding of that item.

Guard against making short-term budget decisions at the expense of longer-term needs. Examples of such situations are unfortunately quite commonplace: spending down fund balances accumulated over a period of time for designated purposes (such as specific capital projects or equipment/vehicle replacement), deferring maintenance

projects, or transferring funds from the general fund to enterprise funds (or vice versa) solely to prop up the fund in question.

Financial Planning and Analysis

A variety of financial planning and analysis tools can provide cities – regardless of size - the necessary information base and guidelines for effective strategic budgeting and planning. They can help policymakers evaluate the short-and long-range impact of budget proposals. They can help elected officials see the big picture and prioritize proposals or projects at the same time, rather than on an individual or stand-alone basis.

Financial Trend Analysis –A city needs to know the state of its financial condition. Periodic monitoring and evaluation of financial data and trends, including multi-year forecasting of revenues and expenditures, can help elected officials think strategically about priorities and needs.

Financial Policies - Financial policies establish guidelines pertaining to key elements such as revenues, operating expenditures, capital expenditures, reserve funds, fund balances, investments, debt management, enterprise funds, accounting, auditing and reporting. Carefully developing and monitoring meaningful financial policies, such as establishing and maintaining fund balances as a percentage of fund expenditures or per capita debt service expenditures as a percentage, can provide very useful guidelines to assist elected officials in making difficult budget decisions.

Capital Improvements Program (CIP) – The CIP is a multi-year (typically three to ten year) program for the planning, scheduling and financing of large construction, infrastructure and improvement projects, and purchasing of major pieces of equipment. The CIP helps prioritize capital spending needs and provides useful information about upcoming major expenditures.

Equipment/Asset Replacement Plan – Similar to the CIP, this is typically a five to twenty-year plan identifying the scheduled replacement of equipment, vehicles, facilities and other physical assets. Like the CIP, it helps policy makers anticipate and plan for upcoming major expenditures beyond the standard one-year budget cycle.

Contingency Planning – During times of financial uncertainty, it can be quite helpful to develop budget contingency plans, especially for revenue shortfalls. Certain revenue sources, such as local option sales taxes, can be extremely volatile during these periods. Developing advance contingency plans allows for more deliberate and careful analysis of alternatives and options as opposed to crisis mode emergency responses.

Stimulating Economic Growth

As discussed in the recent white paper “Navigating the Fiscal Crisis: Tested Strategies for Local Leaders”, prepared by the Alliance for Innovation and ICMA, one of the best methods for cities to stimulate their local economies may be to maintain current expenditures and expand capital improvements, provided local revenues, reserves, interest rates and federal programs make it possible. Of course, these conditions rarely occur during economic downturns. It is more likely that city expenditures get reduced, which in turn may negatively impact economic development in the community.

The white paper suggests that periods of economic distress may be the most opportune time to promote local economic development efforts. Private sector firms tend to be more sensitive to the impacts of economic development incentives, because their profit margins may be smaller and their cash flow more constrained.

Recognizing that direct cash outlay may be problematic for local governments during these downturns, the white paper identifies other opportunities to entice economic development, including infrastructure, skilled available workforce, job training, and educational institutions and streamlining project reviews. Finally, the white paper points out that a period of resource scarcity is an appropriate time for jurisdictions in a region to share economic development incentives and benefits.

Citizen Engagement

Effectively dealing with long-term financial issues is not easy. Difficult decisions have to be made. It is crucial to develop strategies and methods to inform, listen to and involve a broad base of community members in this process. Such an approach benefits both citizens and elected officials.

For citizens:

- They learn more about the issues and decision-making processes.
- An effective citizen engagement process can lead to creating partnerships for solving problems.
- The process allows citizens to provide real input on policy decisions.
- The process can create a strong sense of buy-in and belonging.

For local officials:

- A citizen engagement process can demonstrate to citizens that certain public decisions are difficult and complex.
- The process helps citizens understand the financial pressures that affect services and programs.
- The process helps elected officials find out what citizens really think about important issues and policy decisions.
- The process can help defuse tensions between groups of people and between citizens and government.

Of course, the citizen engagement process is not absolute. Elected officials are still responsible for setting policies and making decisions for the community - and the local elected leadership team is still ultimately responsible for the overall success and vitality of the community – with citizen guidance, input and engagement.

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