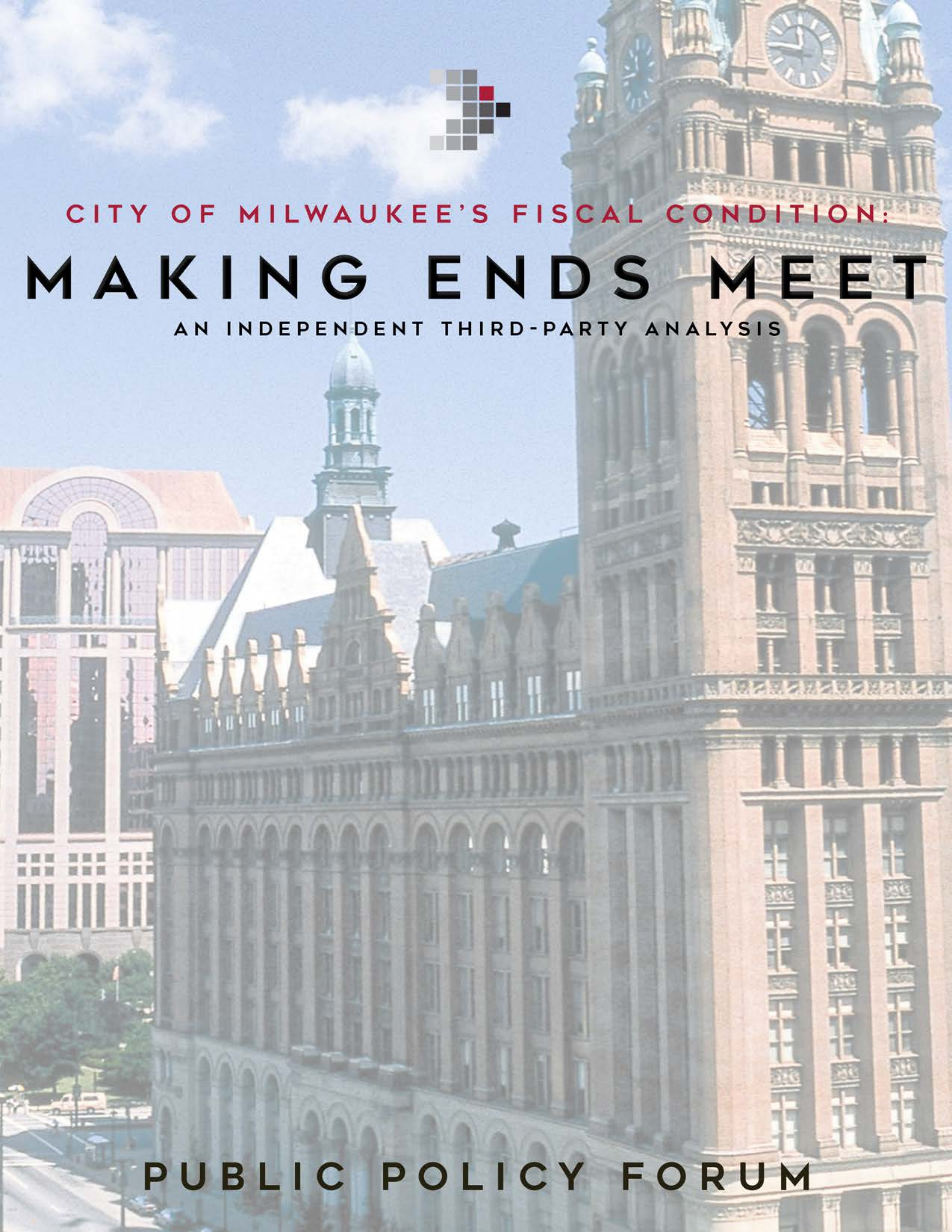
CITY OF MILWAUKEE'S FISCAL CONDITION:

MAKING ENDS MEET

AN INDEPENDENT THIRD-PARTY ANALYSIS



PUBLIC POLICY FORUM

Executive Summary

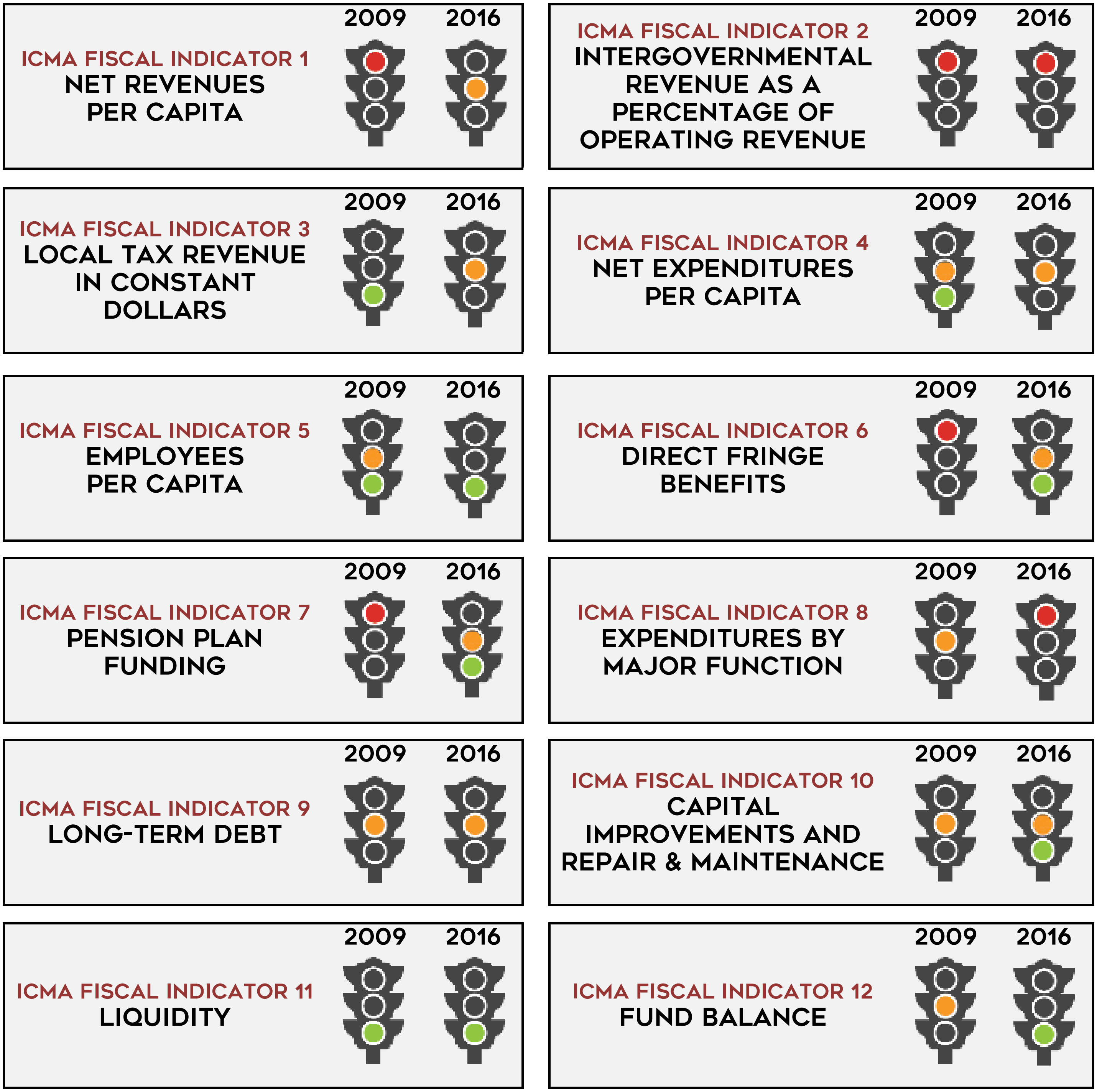
In 2009, the Public Policy Forum's deep dive into the finances of the City of Milwaukee revealed a government with "serious, deep-seated fiscal problems." As suggested by the report's title – "Between a Rock and a Hard Place" – the City found itself in an untenable and virtually unmanageable situation, facing daunting expenditure needs associated with fringe benefits and aging infrastructure on the one hand, yet locked into a revenue structure that yielded little hope for growth on the other.

Today, after conducting another comprehensive assessment of the City's finances, our prognosis is not nearly as alarming. City leaders *were* able to deftly manage their recession-induced challenges, thanks largely to health care restructuring. Changes in the City's health care offerings and administration yielded tens of millions of dollars of annual savings that were used to meet pension obligations, replenish reserves, and spare departments from significant service reductions.

Yet, as shown in the comparison box on the following page, while Milwaukee has made considerable progress with regard to several of the fiscal indicators used for our analysis, two glaring red lights remain. The first is intergovernmental revenue, which consists largely of shared revenue from the State of Wisconsin. This is the City's largest revenue source, but it declined by nearly 4% in nominal terms and 9% in constant dollars over the 2011-2015 timeframe. The second is expenditures by major function, where our analysis revealed that the public safety function consumed $35 million of the City's overall $38 million increase in general purpose expenditures during that same timeframe just to maintain existing police staffing levels.

If, as expected, these contradictory trends of flat intergovernmental revenues and fierce public safety expenditure pressures continue, then it is difficult to see how City leaders will be able to spare non-public safety departments from service reductions, especially when health care expenditures again begin to rise. Furthermore, the City's wherewithal to make and sustain *increased* investment in additional police officers, community development, and/or other measures in response to the recent unrest in Sherman Park will be extremely challenging barring some new source of revenue.

ICMA fiscal indicators, 2009 vs. 2016



Specific findings from our updated assessment of the City of Milwaukee's fiscal condition include:

- **Milwaukee remains far too reliant on property taxes and fees.** A 10 million (3.6%) decrease in intergovernmental revenue from 2011-2015 necessitated a $23 million (14%) increase in property taxes for the General Fund and a $17 million (17%) increase in charges for services to allow overall revenues to keep pace with inflation. Meanwhile, substantial future growth in property-related revenues – even if deemed politically palatable – will be limited by state property tax levy restrictions and the reality that service-related fees only can be used to pay for the services with which they are associated, as opposed to general operating needs.

- **Health care savings soon will be exhausted.** Annual employee/retiree health care expenditures dropped from $139 million in 2011 to $96 million in 2015 (31%). Those savings were central to the City's ability to accommodate a $60 million spike in pension obligations, avoid workforce reductions, and maintain police staffing levels. By 2018, the City again will have to budget for modest annual health care increases, which will exacerbate its other expenditure pressures.

- **Police service needs could threaten service solvency in other areas of City government.** The Milwaukee Police Department spent $59 million more in 2015 than in 2011, even though it had two fewer officers (1,876 vs. 1,878). This was caused, in part, by the need to replace expiring federal stimulus grants with local resources. Maintaining sworn strength levels will not require as big a financial commitment in the future now that grant dollars have been supplanted and police union members contribute to their pensions; however, the pressures associated with replacing retiring officers, modernizing technology, and accommodating natural growth in police salaries and benefits still could crowd out other needs.

- **Retirement liabilities and debt are manageable today but growing.** The City's unfunded actuarial liability for Other Post-Employment Benefits (OPEB) stood at $976 million in 2015, which is $60 million higher than in 2011; and its pension fund – while in far better shape than many cities – still requires an annual contribution of $60 million, a number that could rise beginning in 2018. Meanwhile, property tax levy-supported debt grew from $561 million in 2011 to $629 million in 2015. Increasing retiree liabilities and debt payments can be managed in the short term, but may pose substantial long-term fiscal challenges.

It is important to consider Milwaukee's fiscal strengths, as well. Our analysis reveals that the City has well-stocked reserves and strong liquidity, and that it has made progress in addressing its infrastructure needs. Also, the resilient manner in which City finances emerged from an historic economic recession should not be understated and conveys hope for similar resiliency in the future.

Nevertheless, our 2009 conclusion that Milwaukee needs "fundamental fiscal change" has not been altered. The City's revenue structure – which has been imposed upon it by the State of Wisconsin – remains broken. Until it is modified to reduce the City's reliance on property-related revenue, and to provide wherewithal for total annual revenue increases that mirror the rate of inflation, then City finances will continue to be stressed, and substantial *new* investment in public safety and community development-related programs will be highly difficult to achieve.