Budget Brief:

2015 Proposed City of Milwaukee Budget

Public Policy Forum

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ABOUT THE PUBLIC POLICY FORUM

The Milwaukee-based Public Policy Forum, established in 1913 as a local government watchdog, is a nonpartisan, nonprofit organization dedicated to enhancing the effectiveness of government and the development of Southeastern Wisconsin through objective research of regional public policy issues.

PREFACE AND ACKNOWLEDGMENTS

This report is intended to provide citizens and policymakers with an independent, comprehensive, and objective analysis of the Mayor's proposed City of Milwaukee budget. We hope that policymakers and community leaders will use the report's findings to inform discussions during upcoming budget deliberations.

Report authors would like to thank Milwaukee fiscal officials and staff – including the Budget Director and his staff – for their assistance in providing information on the City's finances.

Finally, we wish to thank the Northwestern Mutual Foundation for generously supporting our local government finance research.

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Introduction

For the most part, the issues confronting City of Milwaukee officials as they prepared the 2015 proposed budget were quite familiar. Faced with limited growth potential in their two major revenue streams (state shared revenue and the property tax), as well as increasing pressure to use property tax resources to address pension obligations and employee health care costs, the challenge again was to determine how to preserve essential city services without depleting reserves or exacerbating long-term funding needs.

The 2015 proposed budget attempts to meet that challenge with a mix of fee increases, contributions from special funds and reserves, health care changes, and increased borrowing for capital improvements. When combined with a modest property tax increase, these strategies allow the City to maintain police and fire staffing levels, address key infrastructure challenges, and continue to grapple with the impacts of the foreclosure crisis. While largely bereft of major new initiatives – with the exception of a new "Compete Milwaukee" initiative to address unemployment – the budget also continues to stay true to a multi-year fiscal sustainability strategy that aims to position the City to meet its long-term retirement and infrastructure obligations.

At the public hearing held to review departmental budget requests last August, the mayor and his budget director accentuated the need to establish spending priorities in the face of declining state aids. Once again, the mayor's proposed budget does that by emphasizing strong neighborhoods, public safety, and public works. But it is another priority in the mayor's budget – the effort to offset the "sacrifices" made by general city employees as a result of higher pension contributions required under Wisconsin Act 10 – that may draw the most scrutiny in an otherwise calm budget year.

A strong case can be made that the proposed 3.9% pay increase and elimination of furlough days for most general employees is justifiable as a means of maintaining employee morale and as a general matter of fairness. But it is because of the City's overall structural challenges, its need to prioritize, and its lack of wherewithal to pursue major new initiatives that this proposal does merit discussion, which we undertake later in this report.

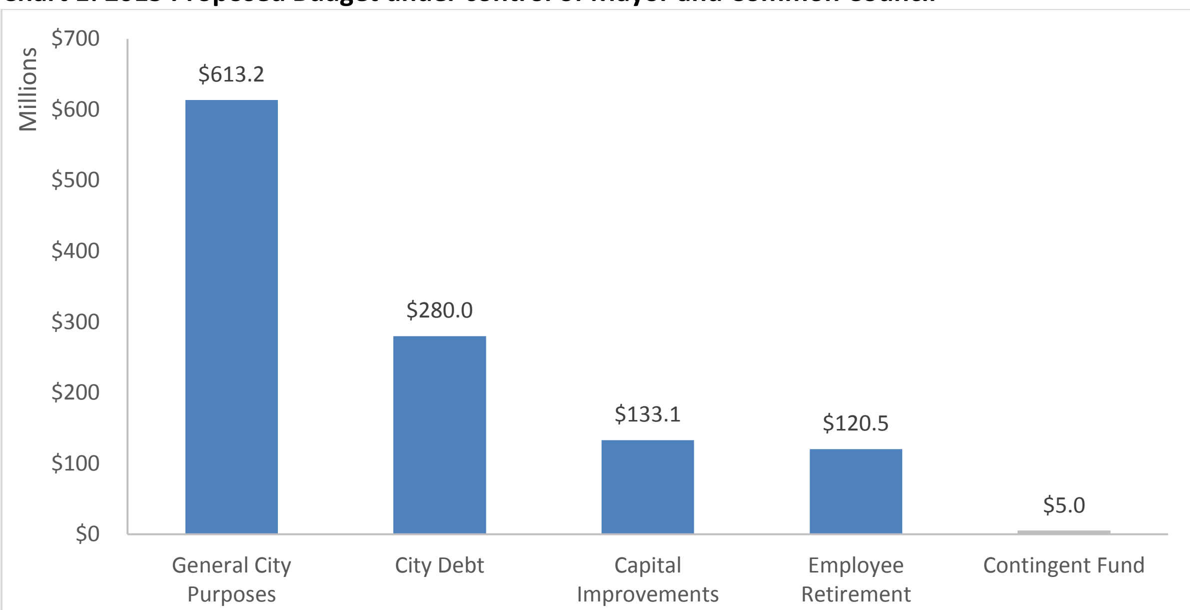
Overall, while it is tempting to pass off the 2015 proposed budget as "status quo," doing so would unfairly minimize the challenges City leaders face each year in accomplishing that seemingly simple objective. As the Forum has pointed out in the past, the City finds itself in a fiscal straitjacket created on the one hand by stagnant major revenue streams over which it has little control, and on the other by fierce expenditure pressures created by vast public safety needs, aging infrastructure, and daunting retirement obligations. The true test is whether the proposed budget is able to maintain immediate service levels while responsibly looking out for the future, and our assessment indicates that it does.

In the pages that follow, we provide more detailed analysis of how major revenue and expenditure challenges were resolved in the 2015 proposed budget, and the manner in which the city has adhered to its key strategic objectives and its multi-year fiscal sustainability plan. Our hope is to provide an independent assessment of the city's fiscal circumstances and outlook that will be used to inform deliberations on its 2015 budget.

Budget Overview: Expenditures

The 2015 proposed budget contains $1.5 billion in expenditures, which is an increase of about $67 million (4.4%) above the expenditure amount in the 2014 adopted budget. Of the $1.5 billion total, about $1.2 billion is under the control of the mayor and common council, as shown in **Chart 1**. The remaining $363 million in expenditures are housed in separate funds that derive their revenues from sources other than the property tax levy, including the Milwaukee Water Works and special funds for sewers and parking. In this budget brief, we focus primarily on the "General City Purposes" component of the budget, which in the 2015 proposed budget totals $613 million, as well as the Employee Retirement section, City Debt, and Capital Improvements.

Chart 1: 2015 Proposed Budget under control of Mayor and Common Council



Source: 2015 Proposed Budget

The proposed budget reflects the continuation of the City's long-term sustainability plan, which provides a multi-year framework to guide budget decisions in a manner that is intended to ensure long-term financial stability and stable service levels, while accommodating increased pension payments and flat state aids. When it was introduced in the 2013 budget, the plan originally identified a structural deficit of $65-$75 million, which could have potentially required the elimination of 600 positions through 2016.

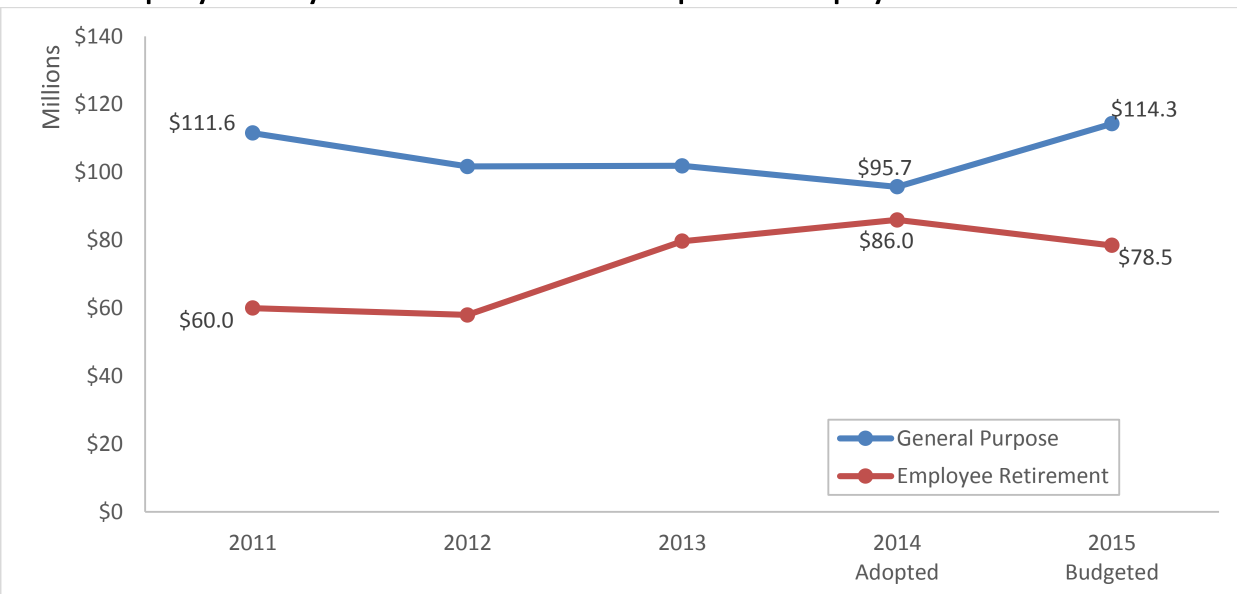
According to the budget document, actions taken during the past two years have reduced the projected structural deficit to $25 million entering 2015. While this reflects substantial progress, the budget acknowledges that additional difficult decisions will have to be made to maintain a sustainable financial model. The 2015 proposed budget does not contain any major program cuts but continues to chip away at the gap, mainly through efforts to achieve greater efficiency in city operations.

Despite efforts to enhance efficiency and control expenditures in virtually all city departments, the 2015 proposed budget does include an increase of $22.5 million (3%) over the 2014 budget for general city services. However, rather than reflecting a substantial increase in staffing or service levels, the majority of this increase reflects the need to accommodate salary and fringe benefit cost increases. Major expenditure changes in the proposed budget are summarized below.

Pension

An effort to realign city finances to accommodate the need for higher pension fund contributions was a major component of the past several City of Milwaukee budgets. As shown in **Chart 2**, since 2012, this effort has resulted in a shift of increasing amounts of property tax levy into the Employees' Retirement Fund and away from general city services. In the 2015 proposed budget, however, that trend is reversed, mainly because all non-public safety employees are now being required to contribute toward the cost of their pensions.

Chart 2: Property Tax Levy Contributions to General Purpose and Employee Retirement Funds



Source: 2015 Proposed Budget and previous budgets

For the past several budgets, the City has not implemented the Wisconsin Act 10 provision requiring non-public safety employees to pay the "employee share" of their pension costs. This decision resulted from a City Attorney's opinion that the City must continue to pay those contributions on behalf of employees. That opinion was supported in District Court but was reversed earlier this year by the Wisconsin Supreme Court, which means that general employees hired before January 1, 2010, now will be required to pay the employee contribution. That will amount to 5.5% of salary for those employees.[1]

As a result of this change, the City is relieved of an $8 million payment to the retirement fund. However, a decision to address the impact on wages by providing most general city employees with a 3.9% salary increase, and to eliminate furlough days for all general employees, essentially shifts those costs to the City's general purpose budget, thus accounting for a substantial share of the expenditure increase in the general budget.

Meanwhile, the proposed budget includes $60 million for the *employer* share of the pension contribution, which is a $1.6 million reduction from 2014 in light of improved actuarial projections. The budget anticipates that property tax levy will be used to cover $49.6 million of that amount, while $10.4

[1] General city employees hired between January 1, 2010 and January 1, 2014 already have been paying the 5.5%, while those hired after January 1 of this year pay 4% because of reduced benefit levels.

million is drawn from the City's pension reserve. As has been discussed in previous budget briefs, the City built up a strong reserve during 2011 and 2012 to help take some of the burden off the property tax levy once the employer contribution spiked to more than $60 million in 2013. A policy instituted by the City and the pension board in 2013 now provides for steady employer contributions of $60 million through 2018. A more detailed discussion of the City's pension fund is provided later in this report.

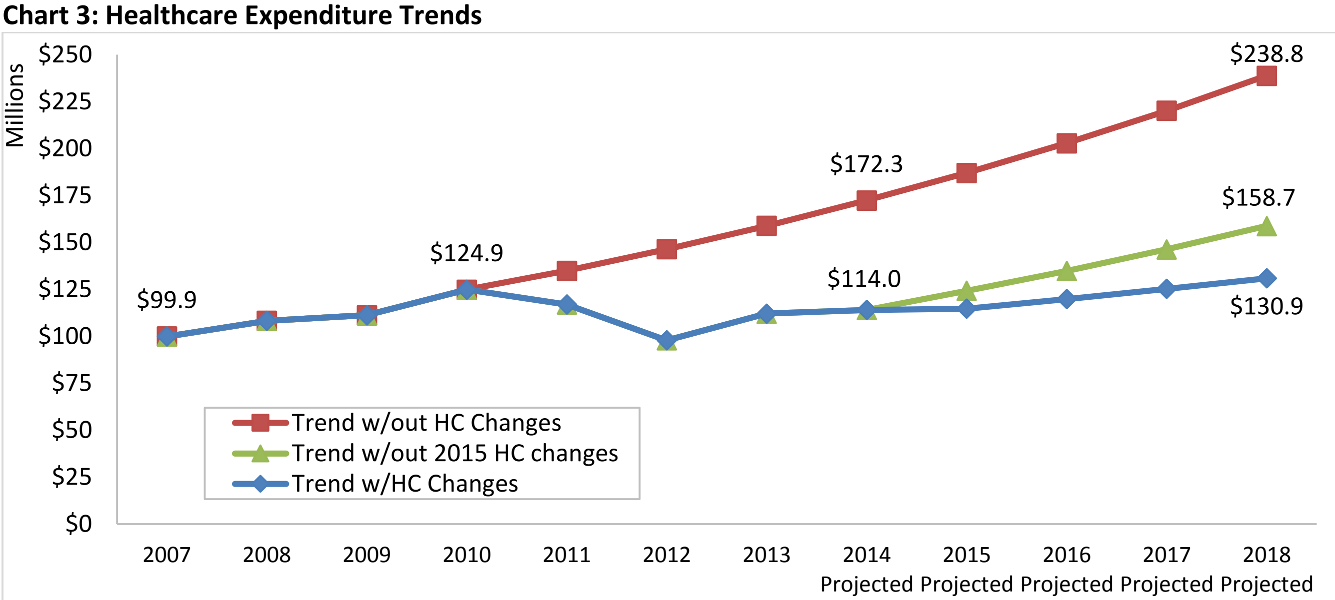
Health care

The implementation of several strategies to reduce and then curb the growth of employee health care costs has been a major component of the City's fiscal sustainability strategy during the past several years. In addition to requiring civilian employees to pick up an increased portion of co-pays and deductibles, the City also moved to a self-insured healthcare plan and has been encouraging employees to make smarter utilization choices and to participate in a wellness program.

Despite these changes, which saved tens of millions of dollars in previous budgets, health care costs were anticipated to continue to increase sharply over the next several years. In response, City leaders adopted additional changes to health care plan design this past summer. Those changes will be implemented in 2015 and result in a $4 million savings from the cost that originally had been projected. They include increased cost-sharing for deductibles, co-insurance, and out-of pocket-maximums.

The impact of these changes can be seen in **Chart 3**. The projected growth in health care costs has been reduced remarkably when compared to 2011 projections as a result of comprehensive changes adopted in 2011 and additional changes in subsequent years, including 2014. Nevertheless, health care expenditures still will rise from the $110 million budgeted in 2014 to $119.8 million in the proposed budget, thus contributing more than 40% of the $22.5 million increase in the general purpose budget.[2]

Chart 3: Healthcare Expenditure Trends



Source: City of Milwaukee

[2] The $9.8 million increase budgeted for 2015 reflects both health care inflation and adjustments that align previous year actual expenditures with budgeted amounts. Also, **Chart 3** reflects a mid-year projection of 2014 health care costs, as opposed to the budgeted amount.

Employee Wages

Each year, the City must grapple with the challenge of balancing its desire to provide cost-of-living increases in compensation to its workforce with competing operational priorities. General city employees did not receive wage increases in 2011 or 2012, while a 1.5% wage increase was provided in 2013 and a 1% increase in 2014. In each of those years, the budget also included three or four furlough days (i.e. mandatory days off without pay) for general city employees. As noted above, the 2015 proposed budget includes a 3.9% wage increase for select general employees,[3] in part to offset the new requirement in 2015 that those employees pay 5.5% of their salaries toward the cost of their pensions. This proposal would increase salary costs by $4.8 million. In addition, the proposed budget eliminates furlough days for general employees at a cost of $2.8 million.

It is important to note that furloughs (three days) remain in effect for sworn public safety employees and that the 3.9% wage increase does not apply to them. Public safety unions are not covered under Act 10, and their compensation will be determined by collective bargaining agreements.

Police Department

The proposed budget continues efforts to prioritize the preservation of police service levels and grows by $4.9 million (2%) from the 2014 budget. This is mostly due to the first full-year impact of 20.5 full-time equivalent employees (FTEs) added to enhance sworn officer strength in mid-2014, as well as projected cost-to-continue increases related to salaries and benefits. Overall, the 2015 proposed budget includes an additional 12 police officer FTEs when compared to the 2014 budget, increasing the number of sworn officers from 1,868 to 1,880. Also, about $250,000 of the $4.9 million increase comes from the elimination of furloughs for civilian police employees. The budget also contains $100,000 to implement the use of body cameras and $842,000 for various equipment replacements.

Fire Department

The proposed budget reduces Fire Department spending by $3.5 million from 2014, largely because of changes involving the accounting for prior year and projected wage and fringe benefit costs for represented employees. While this represents a sizeable expenditure decrease, the department still maintains approximately the same level of FTEs as in 2014. The budget also emphasizes the use of smoke detectors by expanding the FOCUS program. Fire officials will inspect each home and business every five years with the goals of installing and testing smoke detectors in one- and two-family homes, building relationships in the community, and establishing emergency preparedness.

Strong Neighborhoods

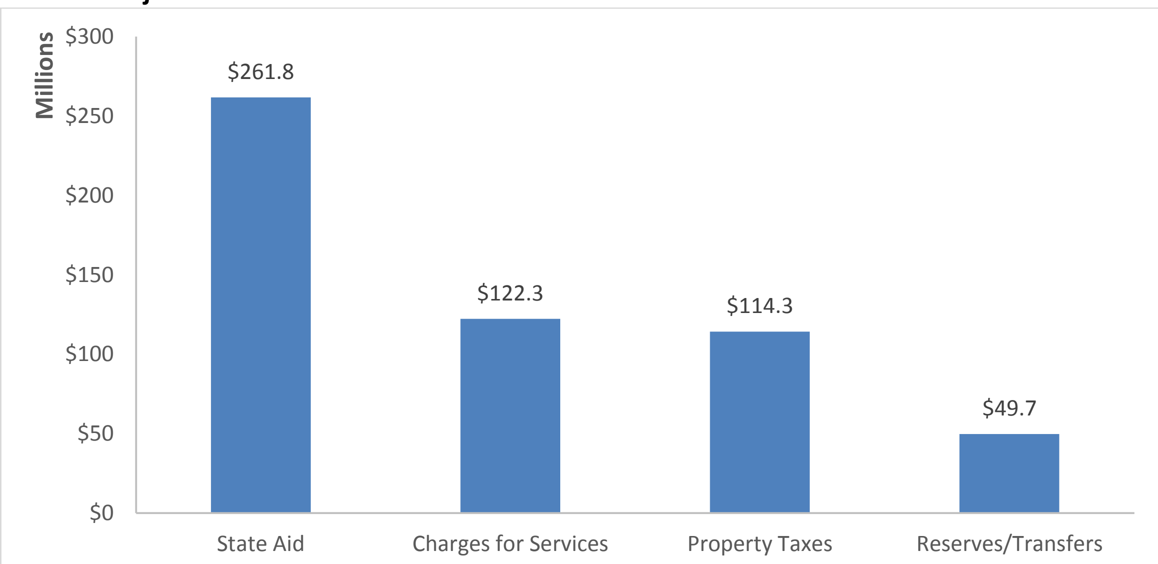
The proposed budget continues to implement the mayor's Strong Neighborhoods Plan, which addresses the City's substantial glut of foreclosed properties through a variety of strategies. The budget includes $10.6 million to support this effort, a decrease of $1.1 million from 2014. A $3.2 million reduction for building demolitions and a $1.9 million increase for prevention and revitalization work illustrates the City's shift toward more proactive foreclosure solutions. Prevention and revitalization activities include deferred loans for low-income and elderly residents with critical home repair needs, incentives for rehabilitations of commercial properties, and a rent-to-own program.

[3] No wage increases are included for 712 employees already contributing 5.5% and 187 workers contributing 4% toward their pensions.

Budget Overview: Revenues

The $22.5 million expenditure increase in the general city purpose budget is offset by an increase of $18.6 million in the amount of property tax levy dedicated to that segment of the budget.[4] The remaining $3.9 million comes from fee increases and increases in state aid. As shown in **Chart 4**, the bulk of general city revenues in 2015 will come from those three sources, as well as transfers from special funds and reserves. Other revenue sources include fees generated from licenses, internal transfers to cover the cost of fringe benefits, fines, payments in lieu of taxes, and miscellaneous revenue sources. The following summarizes significant changes in the City's major revenue sources in 2015.

Chart 4: Major Revenues Sources in 2015



Source: 2015 Proposed Budget

State Aid

Revenue from the State of Wisconsin makes up $261 million, or 43%, of total operating revenue. The City has documented the extent to which its major form of state assistance (state shared revenue) has not kept pace with its expenditure needs over the past decade. In 2004, the City's state's shared revenue allocation from the State was $240 million, but that amount had declined to $227 million in 2014, which represented a 5.4% drop in real terms and a 29.6% decline when accounting for inflation.[5] The City receives only a minimal ($128,000) increase in shared revenue in the 2015 budget. However, in a break from previous years, its total intergovernmental revenue increases by $1.9 million over 2014. This is mostly due to an unexpected increase ($793,000) in transportation aid as well as a $600,000 increase in the computer exemption payment from the State and a $275,000 increase in the Expenditure Restraint Payment.

[4] The total 2015 proposed levy is $257 million, or $3.1 million (1.2%) greater than the 2014 levy. A breakdown of the total levy is discussed later in this section.

[5] These totals include the City's annual Expenditure Restraint Payment, which is a form of shared revenue provided by the State that is only awarded to municipalities that meet certain expenditure restraint criteria.

Charges for Services

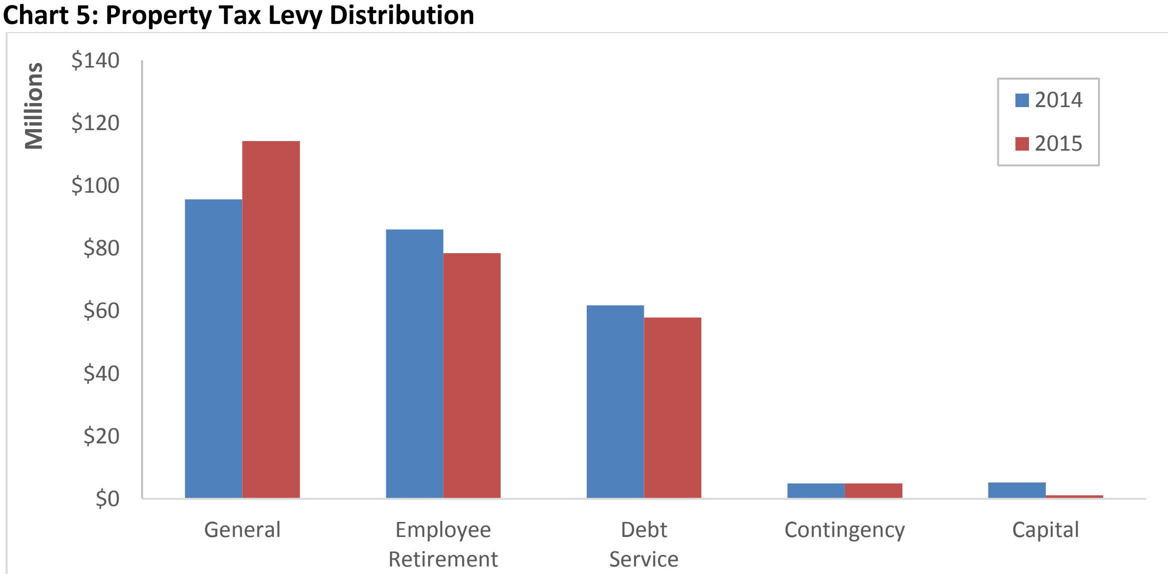
The City generates transactional revenue from various services it provides. Given the decline in shared revenue and property tax levy constraints, City leaders have aggressively sought to ensure that service-related fees cover increases in service costs. In the 2015 proposed budget, Charges for Services make up $122 million, or 20%, of the City's general purpose operating revenue. This is a $4.8 million increase over the 2014 budget. Included in the extra fee revenue is an increase in the Solid Waste Fee (to $194.40 per year for residential units from $187 in 2014) that is linked to increased tipping fees charged to the City. The Snow and Ice Fee also increases to account for increased snow and ice removal expenditures. The budget indicates that municipal fees for the typical homeowner would increase by $16.59.

Property Taxes

The proposed operating levy totals $114.3 million, which is an increase of about $19 million (19%) over the 2014 amount. Overall, the 2015 proposed budget contains a property tax levy of $256.9 million, which is an increase of $3.1 million (1.2%) over the 2014 levy. **Chart 5** compares the proposed distribution of property tax levy resources among major budget functions to the budgeted distribution in 2014. This shows that the amount of levy dedicated to the pension fund, capital improvements and debt service decreased, thus freeing up additional resources for general city purposes.

The proposed property tax levy would increase the City portion of the property tax bill by $4.52 for the typical homeowner. According to budget officials, the proposed budget could have raised the property tax levy by $4-$5 million in 2015 without impacting the state-imposed levy limit and/or the City's anticipated Expenditure Restraint Payment from the State.

Chart 5: Property Tax Levy Distribution



Source: 2015 Proposed Budget and previous budgets

Fund Transfers and Use of Reserves

In addition to these three main revenue sources, the 2015 Budget includes sizable transfers from the Tax Stabilization Fund, Parking Fund, and Sewer Maintenance Fund. The total amount of transfers allocated from these funds is $49 million, or 8% of total operating revenue. A more detailed discussion on transfers and use of reserves is included below.

Key 2015 Budget Highlights

In this section, we provide more detailed discussion on a set of noteworthy issues in the 2015 proposed budget. These issues were selected based on their impact on overall spending and revenues in 2015, their importance in the context of the City's multi-year effort to restore structural balance, and their programmatic significance.

Salaries

In light of the City's ongoing structural challenges, one of the most noteworthy items in the proposed budget is the recommended 3.9% wage increase for certain general city workers. This wage increase ($4.8 million) plus the elimination of furloughs for all general employees ($2.8 million) adds $7.6 million in salary costs to the proposed budget. Those costs are fully offset, however, by the $8 million in employee pension contributions that will be collected from most general city employees beginning in 2015.

City leaders have justified the 3.9% pay increase by citing reductions in compensation experienced by most general city workers during the past several years. Those have included furlough days, increased out-of-pocket health care costs, and the absence of wage increases in 2011 and 2012, all of which were imposed to help balance the City's budget.

In **Table 1**, we attempt to shed light on that justification by showing a broad, simplistic illustration of the impact of wage freezes, furloughs, and the new pension contribution on the take-home compensation of an average City worker since 2010. We start with an assumption that the average general city employee received a salary of $49,326 in 2010.[6] We then adjust the salary amount to reflect wage increases of 1.5% in 2013 and 1% in 2014 after two successive years of freezes. The table also shows a deduction for furlough days each year and, for 2015, the new employee share of the pension contribution.

It is important to note that we do not show health care premiums, which stayed roughly the same, nor do we include health care co-pays, deductibles, and out-of-pocket expenses, which increased substantially for many employees. While those items also have a considerable impact on compensation, they vary by employee and are difficult to capture in a broad analysis. Also, we do not take into account any tax implications from the pre-tax treatment of health care and pension contributions.

Table 1: Compensation for an Average City Employee, 2010 to 2015 (Proposed)

	2010	2011	2012	2013	2014	2015 w/no change	2015 w/increase
Furlough Days	4	4	4	3	3	3	0
Furlough Cost	$759	$759	$759	$578	$583	$583	$0
Pension Contribution	$0	$0	$0	$0	$0	$2,781	$2,890
Total Salary	**$49,326**	**$49,326**	**$49,326**	**$50,066**	**$50,567**	**$50,567**	**$52,539**
Total Adjusted Pay	**$48,567**	**$48,567**	**$48,567**	**49,488**	**49,983**	**$47,202**	**$49,649**

Source: 2015 Proposed Budget and previous budgets

[6] $49,326 actually is the average salary for a general city employee in 2014; we use this amount in our illustration because we did not have access to the average salary amount for 2010.

This rough analysis shows that without a salary adjustment in 2015, compensation for the average employee would be $1,365 (2.8%) lower than that received five years ago. Adoption of the proposed 3.9% increase provides the "average employee" with a compensation increase of $1,081 (2.2%) over the five-year period, though he or she still would receive about $300 less than in 2014. We also calculated how the average employee's gross salary would have changed with annual increases based on the Consumer Price Index, and we found that such adjustments would have produced a gross salary of$53,804 in 2014, as compared to the actual amount of $50,567. Finally, it is important to note that according to information provided by the mayor's office, changes to health care deductibles and co-pays could have added up to $1,000 in out-of-pocket costs for employees during this period (depending on their health care utilization), thus reducing compensation by an additional sum of up to that amount.

The proposed wage increase and elimination of furlough days appear perfectly justifiable, therefore, as a matter of fairness to employees. In addition, because the cost of those measures is offset by the increased employee pension contributions in the 2015 budget, it would be difficult to argue that they worsen the City's fiscal condition.

On the other hand, some might argue that the notion that City workers *must* be reimbursed for the recent sacrifices they have made to accommodate the City's difficult fiscal challenges minimizes the depth of those challenges, which arguably demand such sacrifice. Some might also attest that some or all of the $7.6 million cost of the compensation adjustments – while offset by employee pension contributions – still would have been better used to invest in other priority areas, such as public safety, neighborhoods, or infrastructure improvements. In the end, such arguments involve value judgments on fairness and city government priorities that are beyond the scope of this analysis.

Pension

Heading into the 2008 budget, the City had one of the most secure public pension funds in the nation, with an asset-to-liability ratio of 132%. Consequently, the City seldom had to make employer contributions toward its pension fund, as fund assets exceeded actuarial liabilities and the fund was essentially self-sustaining. However, the economic downturn took a toll on the pension fund and reduced its market value by 31%, which produced an unfunded liability of $713 million and required a $49.9 million employer contribution going into the 2010 budget year.

In 2011 and 2012, no contributions were required, although actuarial projections indicated future annual payments of $60 to $90 million from 2013 through 2016. To soften the impact, City leaders responsibly put aside $43 million during those two years to build up the pension reserve. These funds were to be used beginning in 2013 to reduce the amount of property tax levy required to meet the vastly increased contribution amounts. The plan was to gradually increase the amount of levy funds while decreasing the use of reserves until the fund reached a minimum level desired by policymakers. At that time, the total cost of the pension contribution would be covered by property tax levy.

Heading into the 2015 budget year, the City's pension reserve had a fund balance of $25.6 million. The proposed budget allocates $10.4 million from the reserve, which is $3 million lower than the amount used in 2014. At the same time, because of some unused funds from the 2014 payment and a slight decrease in the amount of the required contribution, the amount of levy required to fund the $60 million contribution increases by only $1.4 million, to $49.6 million.

This relatively small increase in property tax levy funding shows that the foresight of City leaders to build pension reserves continues to pay dividends by smoothing the amount of increased property tax levy needed on an annual basis to pay the employer contribution. The good news is that the reserve is sufficiently funded to continue that smoothing effort in 2016 and perhaps in 2017 as well.

Table 2 shows a hypothetical scenario in which the City continues to use the pension reserve to smooth the impact of increased levy contributions for the following two years, while ultimately maintaining a balance of $5 million. Under this hypothetical scenario, the City would need to identify an additional $3 to $4 million of property tax levy to fund the employer contribution in each of the next three years, which obviously is a far lesser impact than otherwise would have been required. Nevertheless, given the City's revenue challenges, the need to secure even these increasing amounts of property tax levy to fund the pension contribution will continue to represent a significant challenge for future budgets.

Table 2: Hypothetical Scenario of Employer Pension Contribution Funding Sources

	2014	2015	2016	2017	2018
Employer Pension Contribution	$61.6	$60.0	$60.0	$60.0	$60.0
Withdrawal from Pension Reserve	$13.4	$10.4	$7.0	$3.2	$0.0
Total property tax levy	$48.2	$49.6	$53.0	$56.8	$60.0
Already budgeted pension levy	$40.9	$48.2	$49.6	$53.0	$56.8
Additional Levy Support	$7.3	$1.4	$3.4	$3.8	$3.2
Fund Balance	**$25.6**	**$15.2**	**$8.2**	**$5.0**	**$5.0**

Source: 2015 Proposed Budget and previous budgets, as well as Public Policy Forum estimates

Fund Transfers and Use of Reserves

About 81% of total revenue in the general city purpose budget comes from state aids, property taxes, and charges for services. Of the remaining 19%, more than 40% (about $50 million) comes from use of reserves and transfers from special funds. These sources include a contribution from the Tax Stabilization Fund, a transfer from the Sewer Maintenance Fund, and a transfer from the Parking Fund.

The City's reliance on special purpose fund transfers and reserves to support ongoing operations is understandable and defensible in light of its lack of control over other major revenue sources. The use of reserves also reflects the diligence of City leaders in building and replenishing them in a responsible manner. In fact, while bond ratings agencies have expressed concern about the status of the City's reserves in the past, the most recent opinion from the Moody's ratings agencies notes "recent improvement in General Fund reserves."

Nevertheless, such reliance does carry some risk given that there are years in which unanticipated circumstances may prevent the City from appropriately replenishing its reserves, or when needs associated with competing uses for special purpose funds may preclude the ability to transfer anticipated levels to the general purpose budget. If that is the case, then difficult choices could be necessary to replace special purpose fund transfers and reserve contributions in the operating budget. The following is a brief summary of the status of the three major special purpose funds used to fund general city services.

Tax Stabilization Fund

A contribution of $16.7 million is budgeted from the Tax Stabilization Fund (TSF), which is replenished on an annual basis from unexpended appropriations and revenue surpluses. While the proposed transfer is $3.3 million less than the previous year and the TSF maintains a healthy fund balance, it is a challenge to sustain such favorable contributions each year. In fact, budget officials estimate that the fund balance will diminish slightly from $50.6 million to $49.5 million after the 2015 withdrawal and anticipated deposits in 2014. **Table 3** shows the recent history of deposits and contributions from the TSF.

Table 3: History of Tax Stabilization Fund balances and withdrawals (millions)

	2011	2012	2013	2014	2015 Proposed
Balance prior to withdrawal	$29.1	$29.2	$35.0	$59.8	$50.6
TSF Withdrawal	$14.6	$13.8	$14.9	$20.0	$16.7
Change from prior year	12.7%	-6.7%	8.2%	34.2%	-16.5%
Withdrawal as % of fund balance	50.2%	47.1%	42.6%	33.4%	33.7%

Source: 2015 Proposed Budget and previous budgets

The 2015 proposed transfer reflects 33% of total fund balance, which is the same as 2014 and far less than the percentage of fund balance used in the three previous budgets. From 2011 to 2013, the TSF played a critical role in helping to stabilize the tax rate and levy during trying fiscal times. Despite its significant usage in those years, the TSF fund balance grew considerably at the end of 2012 as a result of $39.7 million in surplus funds generated from health care savings and various unanticipated revenues. This has allowed for the larger contributions (from a dollar perspective) in 2014 and 2015, albeit at a reduced percentage of overall fund balance.

Parking Fund

This fund collects revenue from City parking operations and parking meters and is used to maintain the City's parking assets. Historically, a portion of these funds have been transferred to the general fund, albeit at reduced amounts in recent years. The 2015 proposed budget calls for a transfer of $17 million, which is a reduction of $425,000 from 2014. Approximately $15 million of that transfer is expected to be covered by parking revenue generated during the year, while the other $2 million would be covered through fund balance. This will decrease the balance in the Parking Fund from $17.9 million to $15.9 million.

Should the City decrease its transfers from the Parking Fund in future years, it will have to come up with other sources to support general operations. In 2015, budget officials had to find an additional $425,000 in the general purpose budget to replace the reduced transfer, and they have indicated that future annual contributions may have to be reduced to $15 million to maintain fund stability. The possible use of Parking Fund monies to help pay for the operation of a streetcar system may further impede the City's ability to transfer monies from this fund for general city purposes.

Sewer Maintenance Fund

This special purpose fund supports the City's 2,450-mile system of public sewers, as well as related City services that play a role in reducing sanitary sewer overflows. It is funded through sewer and stormwater fees imposed on residents. The primary purpose of the fund is to pay for capital needs associated with the sewer system, though a sizeable annual transfer from the fund also contributes to a variety of public works and forestry services paid for out of the general city services budget.

The 2015 proposed budget calls for a transfer of $16 million from the Sewer Maintenance Fund to the general fund through a payment in lieu of taxes, which is an increase of $900,000 over 2014. Those funds are used mainly to offset the cost of street sweeping, leaf collection, brush collection, and pruning. Of the total $16 million transfer in 2015, $1.4 million is planned to be covered through use of fund balance and the remaining $14.6 million is expected to come from revenue generated during the year. This will decrease the balance of the Sewer Maintenance Fund from $13.4 million to $12 million. While this still is a healthy fund balance, an ongoing concern is the need to balance the use of fund proceeds to support ongoing public works expenses in the general fund with the potential need to use increased amounts of these monies for future infrastructure improvements to the aging sewer system.

Alignment with the City's New Economic Growth Plan

On September 23, 2014 – the same day the mayor presented his proposed 2015 budget – the Milwaukee Common Council adopted a new strategic economic development plan entitled *Growing Prosperity: An Action Agenda for Economic Development in the City of Milwaukee*. The plan lays out 47 action items organized under 12 strategies, which are intended to spur future economic growth.[7] No specific timeframe is given for implementing the plan as a whole, but individual action items are labeled as short, medium, or long-term in nature.

While the plan is brand new, several action items are supported by the proposed budget. The most prominent example is the proposal to create a new program called "Compete Milwaukee," which aims to address the city's high unemployment rate by improving connections between workforce development programs and key growth industries, and by expanding the City's transitional jobs program. The program would address two of the economic growth plan's "short-term" action items.

The budget directs $880,000 to the Compete Milwaukee program. The bulk of those funds would support the expansion of the City's transitional jobs program from 100 positions in 2014 to 130 positions in 2015. The transitional jobs program gives Milwaukee residents with barriers to employment an opportunity to gain skills and work experience through employment with the City's Department of Public Works, Police Department, or Department of Neighborhood Services. A majority of the funding for the transitional jobs program would come from the federal Community Development Block Grant program, with the remainder provided by local sources. In addition, $75,000 would be used for an analysis of the region's current and future labor market and associated workforce development needs, which is intended to better align the city's economic development and workforce development efforts.

Another short-term action item included in the proposed budget is a new program that will provide micro-lending to small businesses through a partnership with the Wisconsin Women's Business Initiative Corporation and a national nonprofit organization called KIVA. The budget allocates $25,000 for that purpose. The program utilizes crowd-sourcing to support small business development, with an emphasis on low-income and minority business owners.

One of the plan's action items that is not fully addressed by the proposed budget is an initiative to "return 500 acres of brownfield land to active, industrial use in 10 years." Although that is a long-term goal, it would require redeveloping an average of 50 acres per year, which sets a very high bar. By comparison, the Menomonee Valley Industrial Center, which is adjacent to Miller Park, is a 60-acre business park that took 10 years to fill. The proposed budget calls for $500,000 in City funding to be dedicated toward brownfields, which is the same as in previous years. Redeveloping brownfields properties, however, generally requires the City to use tax increment financing (TIF) and to secure state and federal grants, so the City's brownfields allocation in the budget is far from the only source of support for those projects.

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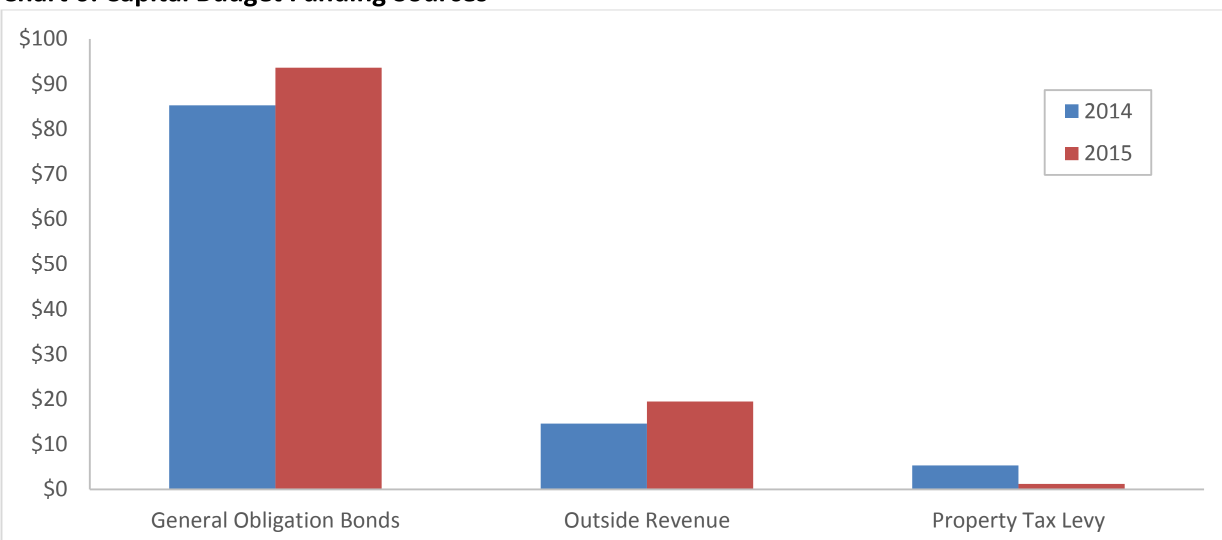
[7] In this section, we seek to illustrate how the economic growth plan is reflected in the 2015 proposed budget. This analysis focuses more on what is reflected in the current year budget as opposed to a comparison to the previous year.

Capital Financing and Debt

As noted above, the capital improvements levy amount decreases in the proposed budget, from $5.3 million in 2014 to $1.2 million in 2015. That decrease is accompanied by an increase in general obligation borrowing and in the use of cash revenues from other sources to finance infrastructure needs. This issue merits discussion given the City's substantial capital needs, which stem from aging streets, sewer lines, and other infrastructure.

Chart 6 shows the breakdown in the three primary funding sources in the proposed capital budget and compares that breakdown to 2014.[8] As shown in the chart, the proposed budget would issue $8.4 million (10%) more in general obligation debt to fund capital projects than in the previous year, which accommodates a $4.1 million decrease in property tax levy.

Chart 6: Capital Budget Funding Sources



Source: 2015 Proposed Budget and previous budgets

The manner in which capital improvement needs are financed in a given year has a bearing on future debt service costs, which are one of the major expenditure pressures in the City budget. In this case, while increased borrowing frees up additional tax levy dollars to support general operations in 2015, the increase also will produce greater debt service funding challenges in future budgets.

Total City debt expenditures are budgeted at $280 million in 2015, which is an increase of $2 million from 2014. Debt service associated with previous year borrowings for the City's capital improvement needs totals $198.1 million, which is an increase of $1.8 million from 2014. (The City also issues bonds on behalf of the Milwaukee Public Schools.) The proposed budget also includes $31.9 million to service debt issued to finance delinquent tax borrowing. While this is a substantial amount, it is actually $1.7 million less than in 2014.

As with capital improvements, the proposed budget reduces the amount of property tax levy required to service the City's debt, from $61.8 million in 2014 to $57.9 million in 2015. This positive development occurs, in part, because of a draw of $8.4 million in unassigned fund balance from the City's debt service

[8] The total 2015 proposed city funded capital improvements budget is $133.1 million and also includes funding from Tax Incremental Districts and special assessments.

fund (a draw of $7 million was made in the 2014 budget). Using unassigned fund balance for this purpose is not an unsound fiscal practice, but it does have the potential of creating additional strain in future budgets if such balances are not similarly available.

The City also possesses a healthily-funded Public Debt Amortization Fund (PDAF) that is available to reduce the tax levy required for debt payments. The proposed budget calls for a withdrawal of $5.5 million from the PDAF. This is an increase of $500,000 from 2014 but, in light of the growth in the PDAF from a balance of $43.5 million in 2001 to its current balance of $56.8 million, this is not a cause for concern.

Overall, the existence of healthy debt reserves minimizes short-term risk that required debt service payments will create undue pressure to increase property tax levy support for that purpose. Nevertheless, heavier reliance on borrowing to address the City's daunting infrastructure needs – combined with increased use of the debt reserve and PDAF – may not be sustainable over the long term. If that is the case, then additional property tax resources may need to be diverted from general operations to support capital and debt service needs, thus exacerbating operating budget pressures.

Capital Budget

The total City-funded capital improvements budget is $133.1 million, which is an increase of $9.7 million over the 2014 budget. As discussed above, the bulk of the funding comes from general obligation borrowing totaling $93.4 million. Major proposed capital expenditures in 2015 are summarized below:

- Core infrastructure improvements total $82 million. This includes funding for streets, bridges, street lighting, and sewers. While the proposed expenditure in this category is a decrease of $3.6 million from 2014, the City has increased annual spending on such infrastructure improvements by $39.4 million since 2004.

- The budget proposes spending $27 million to construct, improve, or renovate city facilities. Approximately one third of this allocation is for improvements to existing public libraries and ongoing replacement of several branch libraries. Other projects include funding for the Fire Department's Fire Repair Shop, remodeling the City Attorney's Office, and upgrades to Public Works facilities.

- A total of $9 million is proposed for system upgrades, including the Police Department's Records Management System, the tax collection system, a new assessment system, and the replacement of voting machines.[9]

- $4.7 million is dedicated to the Strong Neighborhood program. This funding will be allocated toward the demolition of 170 homes, which is a considerable decrease from the 500 in 2014. As noted above, this reflects a shift in priority from demolition to prevention and revitalization activities.

[9] The City also has negotiated a tentative agreement with Milwaukee County to take over programming responsibilities for elections equipment in all 19 Milwaukee County municipalities. If finalized, that agreement should produce additional revenue for the Election Commission.

Conclusion

The 2015 proposed budget once again reflects a prudent and disciplined approach to managing the City's structural challenges. Through a combination of modest property tax and fee increases, steady use of reserves, and concerted efforts to hold the line on departmental expenditures, the mayor and his budget team are able to meet the City's pension and health care needs without reducing services or resorting to unsound fiscal practices.

The proposed budget also makes room for a new workforce development initiative and continued investment in strategies to combat the foreclosure crisis, while maintaining existing police and fire staffing levels and limiting cuts in other areas. Most general City workers also benefit from a pay increase that is designed to provide some relief for increased obligations to pay for the cost of their pensions.

While we raise questions about the long-term efficacy of several elements of the budget's overall approach, that should not be mistaken for concern about the City's fiscal management. On the contrary, our concern stems from the seemingly unsustainable nature of the City's overall fiscal structure, which continues to be plagued by overreliance on flat state revenue streams, coupled with pressing infrastructure needs and retirement obligations that show little sign of abating.

This predicament does raise the question of whether more might be done to improve the City's revenue outlook. For example, the proposed budget makes brief mention of a process currently underway to examine City assets and explore the feasibility of selling ad space, naming rights, and sponsorships to generate additional operating revenue. Another idea considered several years ago – but met with fierce opposition from various parties – was to explore a lease of the City's water utility to increase cash flow that could help meet operating needs. The City also has discussed potential opportunities to sell water to neighboring communities. While none of these ideas are panaceas and each carries with it several potential causes for objection, these may be the types of solutions that will be required to supplement existing revenue streams and cover future expenditure needs.

Perhaps the bigger question to consider is whether City leaders should attempt to use the same strategies they have effectively deployed to meet recent severe challenges year after year; or whether, instead, there is a need for radical changes to the City's fiscal paradigm. If such changes were to involve modifications to the existing revenue structure – such as authorization for new local sales tax authority – then state assistance would be required. Ironically, the City may be its own worst enemy in generating such assistance, as its annual successful effort to balance the budget without undue burden on taxpayers and services diminishes the perception that there is a structural problem at all.

Overall, the City appears poised again in 2015 to effectively manage its way through its perennial set of fiscal challenges. That is good news for the near term, but it should not mask the underlying structural issues that continue to inhibit investment in new programs and infrastructure, and that will continue to pose serious challenges until they are resolved.