



LEXINGTON - FAYETTE URBAN COUNTY GOVERNMENT

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Mayor Jim Newberry Budget Address

Introduction

Members of the Council and Fellow Lexingtonians:

Last Thursday morning, I heard Governor Beshear talking about the budget adopted by the state legislature. He said, "It's not a great budget, but in these times, there are no great budgets." He was right. What I present today is not a great budget, but it is a reflection of the times which confront our city, our state and our nation. The scope of the financial problem confronting our city is significant, and as a result, I have found it necessary to exclude many worthwhile projects and services from the budget which I propose today. Those decisions have been painful, but they were made after countless hours of consideration and thought about which matters were critical to Lexington's future and which expenditures could be set aside for this year.

Today, I want to share with you our proposals for moving Lexington forward – even in tough financial times. These proposals include funding for both operations and for capital investments. I will conclude by identifying several areas where we must work to address some issues which, if left unattended, could cloud Lexington's future.

As we begin, I want to express my appreciation to the commissioners, the chief information officer, the senior advisor for management and my chief of staff for their creative and persistent assistance in preparing this budget. As always, their help has been superb. This year, a special thank-you is also in order. Our Senior Advisor for Policy and Budget, John Cubine, has done an outstanding job developing this budget. He is the consummate public finance professional, and

his help has been invaluable. Last but not least, thanks to all of the staff in the Office of Policy and Budget who provided answers to all of our “what if” questions over the last several weeks.

Scope of the Problem

As you recall, in late February, we believed that we were facing a \$5-7 million shortfall in FY08 – a shortfall which is manageable in light of the hiring freeze and other cost-cutting measures we have employed throughout this fiscal year. In February, we also believed that we would be \$25-30 million short in FY09 if we continued spending at FY08 levels. However, by the middle part of last month, it was our conclusion that if we continued to provide the same level of service in FY09 as in FY08, we would have a shortfall of more than \$35 million or approximately 12% of the FY08 general fund. That dilemma arose for a variety of reasons.

As you recall from last year’s budget address, we began the year with a structural imbalance of \$13.5 million – surplus funds from FY07 that were used for operating expenses in FY08. During the current fiscal year, we have seen revenue stagnate at levels sharply below normal growth rates and below the growth rates projected for this fiscal year. At the same time, expenses over which we have little or no control, such as utility and fuel costs, have risen for LFUCG, just as they have for many Lexington families.

We are also confronted by contractual obligations for sworn personnel and by the prospects of paying accumulated benefits to a significant number of new retirees this year as a result of changes anticipated in the state’s County Employee Retirement System. Finally, our obligations to address storm water issues under the EPA consent decree are timed such that we will need to anticipate expending approximately \$3 million prior to the time at which a storm sewer fee could be implemented.

In future days, we will have occasion to discuss the reasons for the projected shortfall, but for now, suffice it to say, we faced a \$35 million problem which we addressed in order to balance our FY09 budget. We all know there are only three ways to solve such a problem: increase revenue, decrease expenses, or some combination of the two. We have opted for substantially decreasing expenses in conjunction with increases in revenue from four specified sources. In total, those fee increases will generate approximately \$5 million in new funds while the remaining \$30 million shortfall will be addressed through reductions in expenditures and other measures designed to keep Urban County Government living within its means.

We have approached this task on the basis that there should be no broad-based payroll or property tax increase. With the imposition of our sanitary sewer fee increase and the school board’s property tax increase, and with the prospect

of our having to impose a storm sewer fee in the near term, it was not reasonable to ask Lexington taxpayers to pay more payroll or property taxes. While a 0.25% increase in the payroll tax would generate \$16 million in badly needed revenue, we have rejected the temptation to make such a request because we believe that we must make every effort to use existing tax revenue wisely before asking for such a large increase from so many taxpayers.

Matters Left Unaddressed

That decision has left many significant matters in our community unaddressed. The budget which we propose continues to have a structural imbalance. While we have progressed from an imbalance of \$13.5 million in FY08 to an imbalance of about \$10 million in FY09, I remain uncomfortable with this aspect of our budget. Next year, I hope we will be able to significantly reduce or eliminate the structural imbalance.

As I mentioned in the 2007 State of the Merged Government Address, we have massive deferred maintenance issues on many of our buildings. You may recall that last year we added \$500,000 to the Building Maintenance budget to begin to address this issue, and we added an additional \$500,000 to the Parks and Recreation budget to address maintenance issues in our parks. We will continue this funding level during this fiscal year, but this budget does not begin to adequately address our deferred maintenance issues, and I remain concerned that these problems will only worsen and grow larger in the days ahead. In the coming years, either we must materially reduce the number of buildings we own and maintain or substantially increase the sums we are devoting to maintenance. I hope to work with the Council to identify properties that should be declared to be surplus so that they can be sold and the proceeds can be used to improve the maintenance on our remaining buildings.

I am also concerned that we are not expanding the size of our police force and our fire department. Due to the budget constraints, I am recommending that we not hire the 25 new police officers or the 12 new firefighters that had been authorized for this spring due to the impact those new officers and firefighters would have on the FY09 budget. I continue to believe these personnel should be hired at the earliest possible point, and if revenue proves during the year to be stronger than projected, I will recommend to the Council that those classes start promptly.

I could continue with a multitude of needs which this budget will not address. However, we must recognize that no budget will ever address all of the legitimate needs which confront Lexington, and so, with that perspective, let me share with you the results of our efforts to strike a balance between the available resources and our critical needs.

Proposed Allocation of Resources for Daily Operations

Allow me to describe the proposed budget in three areas: decreased spending, increased fees and policy objectives.

To balance the \$35 million initial budget shortfall, we have proposed an assortment of expense reductions, including the following:

- A reduction in the general fund workforce by about 180 employees below current levels during calendar year 2008, resulting in a net savings of \$5.2 million in FY09. The calculations that underlie these numbers are relatively complex, and during the course of the budget hearings, we will be able to explain them in greater detail. For now, please know that we are relying primarily on significant retirements and normal attrition to attain this reduction in force. If we have fewer retirements or less attrition or if our revenue falls short, we will have to implement a layoff plan in order to achieve the savings necessary to balance the budget.
- A 10% reduction in FY08 operating expenses, subject to adjustments in selected divisions, a savings of \$1.5 million.
- A 10% reduction in overtime and seasonal employee expenses, other than fire, corrections and parks, a savings of \$330,000.
- A 10% reduction for most partner agencies, other than the Social Service partner agencies, a savings of approximately \$426,000. The Social Service partner agencies have been exempted from cuts because of my belief that they perform critical services which we should not reduce during an economic downturn and because they play critical roles identified in our recent social service needs assessment.
- A reduction of \$432,000 by transferring the Day Treatment Center operations to the Fayette County Public Schools.
- The generation of approximately \$300,000 from the sale of surplus vehicles currently maintained in our fleet of cars and trucks and from the elimination of expenses associated with those vehicles.
- A reduction of \$1.4 million by suspending for FY09 the World at Work pay increase for remaining employees and by providing a 2% increase within existing grades effective January 1, 2009. World at Work would dictate a 3.9% increase, an increase substantially in excess of a cost of living adjustment. By limiting the increase to 2% effective January 1, 2009, a total of 27 jobs will be saved.
- A reduction of \$600,000 in our general fund contribution to our self-insurance fund over FY08's funding level. Thanks to some truly superb

efforts by both the attorneys in our Department of Law and our outside counsel, we have worked through an assortment of difficult pieces of litigation. Although new claims continue to arise, I feel confident that we can reduce the normal general fund contribution to the self-insurance fund without undue risk.

We have proposed an increase in four fee areas:

- The first proposal is to create a minimum business license fee of \$100 per application. Businesses will receive a \$100 credit on their local taxes so that for those businesses owing \$100 or more in local taxes, there will be no impact. However, there are hundreds of businesses filing for licenses, yet they generate no revenue for the community. In those instances, the fee will serve to pay for the cost of administering the program or will serve to discourage businesses which are not active from filing for a license. In FY09, this fee will generate approximately \$2.7 million, and in subsequent years, we anticipate that it will add approximately \$1.4 million each year.
- We propose to increase EMS fees. Most of these fees are paid by insurance providers, Medicaid or Medicare. Further, our EMS fees have been lower than those in several surrounding communities, and this adjustment will bring Lexington more in line with the going rate for EMS services. The increase would yield approximately \$784,000 next year and more in succeeding years.
- We propose to increase E-911 fees by \$0.79 per telephone line per month. Again, our fees have been lower than fees in several surrounding communities. We will also be exploring more equitable means of collecting rather than billing based only telephone landlines. The increase would yield approximately \$1 million per year.
- Last, we propose to increase several fees in our parks and recreation area. Our recreation fees, if adjusted, will contribute slightly more than \$800,000 in new revenue during FY09.

Those decreases in spending and increases in revenue will help us narrow the financial gap which confronts us, but the budget is also our most significant policy document. A budget should not simply maintain the status quo, but rather it should set the priorities for our city. Despite the economic downturn, we are attempting to use the budget to foster several policy objectives – most of which I hope will sound familiar to everyone present this afternoon:

- We must continue to protect our environment. Most of my comments today have reflected issues relating to the general fund, but there are a number of initiatives relating to the environment that will be paid out of the sanitary sewer user fee and from the so-called “garbage tax”. With

access to these two sources of revenue now and with the prospects of a storm water fee later, I remain optimistic that despite the financial woes afflicting the general fund, we will remain able to make good progress in meeting the requirements of the Consent Decree and improving our environment. We have included \$3.4 million in stormwater projects and \$54.6 million in sanitary sewer projects. We have also proposed a \$50,000 fund for neighborhood environmental projects which neighborhood associations can access in grants of \$2,500 for neighborhood environmental efforts.

- We must continue to enhance our economy. As we have previously discussed, when 83% of our general fund comes from taxes tied directly to our local economy, we must find ways to make Lexington's local economy prosper. Our Bluegrass Business Development Partnership with Commerce Lexington and the University of Kentucky remains a high priority, although like many other aspects of LFUCG, our commitment to Commerce Lexington has been reduced by 10%. We have continued to place a strong emphasis on the arts, a critical component of our economic development strategy in the future. Finally, I remain committed to helping prepare our workforce in the future by providing scholarships to our high school students who major in science, technology, engineering or math majors. We have included \$500,000 to support this initiative during FY09.

I know that many of you have reservations about starting a new initiative in the middle of tight budget times. However, when our general fund revenue is so dependent on taxes tied directly to the strength of our economy, we must take aggressive steps to develop our workforce so we can attract the high tech jobs of the future. I also know that \$500,000 sounds like a lot of money, and it is, but is only about 0.2% of the general fund. I cannot think of a better way to spend 0.2% of the general fund than by investing in our high school students while at the same time sending the world a message that Lexington actively supports science, technology, engineering and math or STEM education. I look forward to working with you to make STEM scholarships available to our kids.

- We must complete our efforts to develop a community vision. Destination 2040 has progressed well as a result of the support which you provided last year. This year, we anticipate bringing the first phase of that project to a conclusion. We are requesting \$40,000 to complete that initiative during FY09.
- Innovative planning is another area of emphasis. In FY08, we committed almost \$600,000 to enhance the day-to-day operations of the Division of Planning and to provide small area plans for the central sector and the Third Street corridor. Those small area plans require enormous work, and we believe that last year's funding will enable us to complete those plans

during FY09. However, we are pleased to propose the inclusion of almost \$540,000 in this year's budget for planning initiatives by the Division of Planning.

- Enhanced communications is a fifth focus. With the creation of the Office of CIO early last year, we have made significant strides in improving the coordination of our information technology and government communications efforts, with new programming underway on GTV3 and expanded customer service in LexCall. We are also seeking authorization to enhance the interoperability of police and fire communications – communications which can be vital to our community during times of emergencies. Further, we are requesting authorization to proceed with the construction of the regional Emergency Operations Center during the next fiscal year – a facility that will be, at its core, the communications hub for the entire community when emergencies inevitably arise.
- Effective government is the sixth objective. As you will see, we have proposed the implementation of several of the Management Partners recommendations, but the vast majority of the recommendations requiring council action should be addressed after the resolution of this difficult budget. Nevertheless, let me address a few of the recommendations which have been the object of much attention from the community.
 - We propose the consolidation of the building maintenance into a new Division of Facilities and Fleet Management. This new division will manage all of the real estate assets of LFUCG to create a more efficient and cost effective process.
 - We propose the elimination of the expenses associated with the Office of Citizens' Advocate. Both the 1998 Charter Review Committee of the Lexington Chamber of Commerce and Management Partners have recommended this action for substantially similar reasons, and we endorse those recommendations in this budget.
 - We do not propose the elimination of currently filled positions in Risk Management. We have proposed that the individuals affected by that recommendation be temporarily reassigned to General Services during FY09 to assist in compiling a comprehensive list of maintenance projects on our real estate assets.
 - We do not propose in this budget decreasing the number of personnel on EMS units from 3 to 2, but that concept is one which should be evaluated in coming months to determine whether such a change is wise.

- We do not propose the closing of any parks, pools or golf courses.

We may revisit some of these recommendations at a later date, but the budget raises enough difficult issues for now. After July 1, we will have ample time to address other recommendations.

In addition to addressing the six pillars, we also propose funding to hire and equip 6 new animal control officers and 3 support staff members. I regret that we were unable to act on this request earlier, but despite the financial constraints imposed by our revenue shortfall, we still need to make progress in addressing at least some of our constituent concerns. I am glad that we can do so now.

Capital Items

As is the case with our operating budget, our capital budget suffers this year. Many worthwhile projects – especially building maintenance projects – are not included, but we have tried to address the critical needs. We propose the following items be funded:

- \$6,000,000 for the redevelopment of the Lyric Theater.
- \$5,500,000 for the implementation of the human resources component of our software system - a critical component of our efforts to overhaul our human resources structure.
- \$2,466,281 for PDR – an increase of about 23%. Although we have traditionally provided only \$2 million in PDR funds, additional matching funds are available, and this increase will enable us to maximize the available matching funds.
- \$1,000,000 for continued construction of our system of bike and walking trails, in addition to continuing our program of providing shared use facilities on existing roads and streets wherever possible.
- \$250,000 for parks parity. For the second year, we are providing \$250,000 to help bring our weaker parks up to the high level of maintenance that we expect of all parks. During this fiscal year, we have undertaken projects at Castlewood, Dunbar, Whitney Young, Marlboro, Martin Luther King, Oakwood, Wildwood, Wolf Run, Lou Johnson, Speigle Heights and Jacobson, and we have projects being designed and reviewed at Masterson Station, Ecton and Smith Street. While I am pleased with our start, we all know we have more work to do, and the parks parity funds will continue our efforts.

- \$150,000 to rebuild the decrepit tennis courts at Glendover Elementary School and \$250,000 to begin repairing other LFUCG tennis courts.
- \$50,000 for a manhole machine. This investment will provide us all with smoother rides as we bring the manholes in our streets closer to grade level.
- Approximately \$3,500,000 for public safety equipment purchases.

These traditional capital expenditures, together with similar capital items too numerous to mention, will keep us within the normal range of bonded indebtedness for this fiscal year. However, I want to recommend that we increase our debt limit for one specific purpose.

We propose that LFUCG issue approximately \$70 million in bonds to provide an injection of capital into the Policemen's and Firefighters' Retirement Fund. As you know, we face a \$230 million unfunded liability. We are obligated to pay 18% of the police and fire sworn payroll to the fund, and we are currently paying an additional 9% in an effort to pay down the unfunded liability. Unfortunately, in the past, our extra funding has only slowed the rate at which the unfunded liability has grown, so despite having made an extra payment of about \$5 million this fiscal year, our unfunded liability is almost sure to grow. That trend must be reversed. Fortunately, by applying an amount equal to that 9% payment to debt service, we can reduce the unfunded liability this fiscal year by approximately \$70 million. If you agree to such an approach, it is fair to say that we will have done far more than any of our predecessors to address the burgeoning financial problems created by the police and fire pension plan. I had hoped to do more, but both revenue constraints and our inability to alter the statutorily-set benefits for new hires leads me to believe that this step is an appropriate intermediate action until such time as we are able to modify our benefit structure for new hires so that our new hires will have the same benefits as virtually all other local police officers and firefighters in Kentucky.

Future Issues to Consider

The preparation of this budget has been in many respects an exercise in frustration. We have many obstacles to overcome and limited financial resources to use. So I want to offer a handful of items which we will need to consider in the short to intermediate future.

- Due to employee confidentiality requirements, we have been unable to confirm our estimate of the number of employees who will retire during FY08 and FY09. Further, we do not know when they will retire or what set of benefits we will be required to pay as those benefits are cashed out. Thus, while we have budgeted \$2 million to pay benefits in FY09, we believe that as much as \$4.4 million more could be required, and those

funds might be required during FY08 if employees retire prior to June 30, 2008. If we are required to cashout benefits to retiring employees in FY08 or if amounts in excess of \$2 million become due in FY09, we will request authorization to apply economic contingency funds to address our cashout obligations.

- In light of the financial constraints facing us the remaining portion of this year and next, we are requesting your authorization to suspend payments to the economic contingency fund for the remainder of this year and throughout FY09.
- Our revenue is over-concentrated on the withholding and net profits taxes. We have heard some of you propose during our budget preparation period that we create a public safety taxing district to be funded by a property tax, and some have suggested that we simultaneously eliminate the so-called "garbage tax" and replace it with a fee for service. Time did not permit us to fully explore that option, but I would welcome the chance to work with you in the next couple of months to determine if such an arrangement can work, especially if the end result is revenue neutral.
- We have far too much real estate, and the utilization of our downtown facilities must be scrutinized. We cannot, due to financial constraints, make much progress on our downtown issues this fiscal year in the absence of a significant rebound in revenue. However, if at all possible, we must fundamentally reassess our real estate holdings, and begin to make the moves necessary for us to have more space and energy efficient facilities and for us to play a significant role in downtown redevelopment.
- Finally, let me share some potentially good news. I learned yesterday that our revenue for March was stronger than anticipated, although we are still behind budget. That news follows a positive February. Whether these two months are harbingers of the end of our economic downturn or merely an aberration is yet to be determined. However, prior to your approval of the budget, we will also know the revenue received and expenses incurred in April and May, which may prove useful in your final determinations.

Conclusion

I wish this budget address could be more pleasant, but I hope two themes have emerged. First, these tight financial times present us with an opportunity to thoroughly scrutinize every expenditure, and we have attempted to do that. However, as I said last year, this is an imperfect budget prepared by imperfect people, so I am confident that you will find oversights and issues which need further attention.

Second, we have to move our community forward, especially in tight financial times. It is not as easy as when money is more accessible, but there are still ways to do it if we are creative. I ask for your support in insuring that Lexington continues to progress, even when our revenue slows and some uncontrollable expenses continue to grow.

The members of my administration stand ready to work with you during the next two months to search for the best means by which to appropriate the funds which the citizens of Lexington have entrusted to our care. In light of your commitment to the community, I am confident the end result will be a product that serves our community well.