

# **Five Year Financial Plan**

## **City of Pittsburg, Kansas**

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### ***Introduction:***

Local governments will always face serious challenges from external forces that include natural disasters, policy changes from other levels of government, and economic downturns, just to name a few. It is the role of governing bodies, management, and finance officers to find ways to not just overcome, but thrive in this type of environment. A long-term financial plan is an important tool that can assist in accomplishing this goal.

There are several reasons to prepare a long-term financial plan.

- Long term financial planning is a key factor in creating an organization that can not only survive but thrive during economic challenges.
- Rating agencies tend to increase bond ratings for those entities with a long-term financial plan in place.
- A long-term financial plan assesses the implications today's decisions have on future financial viability.
- A long-term financial plan assesses programs and services that may be offered.
- Long -term financial plans can help develop strategies to achieve goals and objectives.

A financial forecast is a tool used in developing a long-term financial plan by estimating future revenues and expenditures and identifying the factors which impact them. This forecast is intended to help formulate decisions that encourage financial stability while delivering essential community services.

The information in this forecast includes an analysis of major revenue sources and uses for the primary government and its enterprise funds. The estimates include both quantitative and qualitative information. Quantitative estimates are based on historical data and trends, as well as economic conditions that may impact the City's ability to collect or generate revenue. The qualitative estimates are based on the experience and knowledge of finance staff that will indicate the most likely outcome.

Financial forecasts include a lot of economic variables that can and do change frequently. Other things that will affect the accuracy of the forecast include operational changes, the timing of large capital projects, and policy changes.

***Executive Summary:***

The City constantly looks for ways to maximize limited resources in order to address the priorities set by the City Commission. The current priorities were the result of the 2030 Visioning process. This effort involved one-on-one interviews, focus groups, written surveys and town hall meetings. The result was a list of priorities which would allow the City to attain the overall vision of where Pittsburg should be in the year 2030. Four core areas were identified as critical and are the focus of the implementation plan going forward. These goals continue to be a priority in the 2014 Budget and subsequent years through 2018. They are:

- Housing
- Economic Development
- Infrastructure Improvement
- Public Wellness

In addition to the goals established by the Vision 2030 process, the following goals were identified by the City Commission and Executive Team:

- Rebuild reserves to a minimum acceptable level
- Establish and maintain a Debt Management Plan

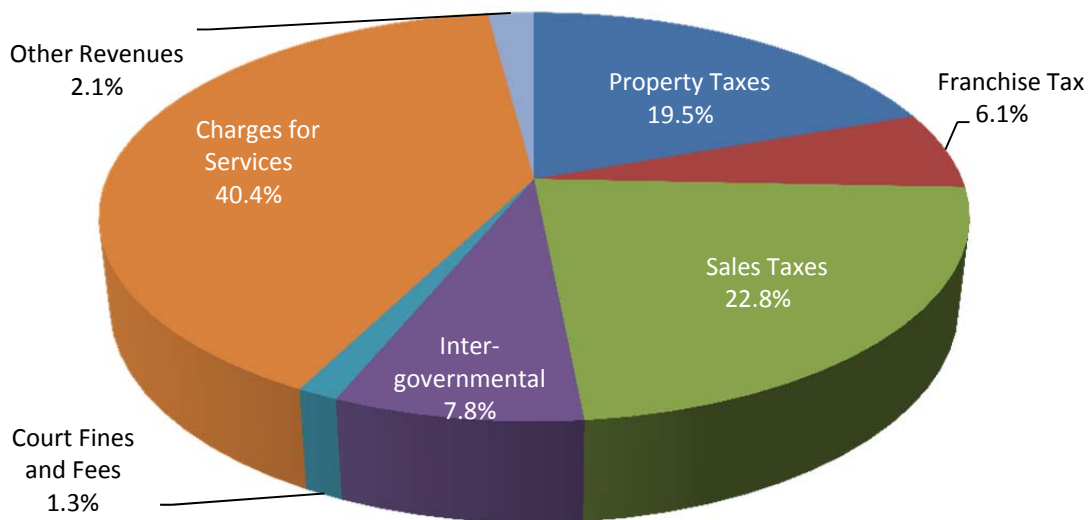
The following discussion identifies major sources and uses of the resources available to the City to accomplish these goals, as well as, potential challenges that will need to be overcome.

## REVENUES

As with all levels of local government, the City of Pittsburg has been adversely affected by the reduction of property values, reduced sales tax, reduced funding from higher levels of government, and other reductions of revenue due to the Great Recession.

While the City of Pittsburg receives revenue from a variety of sources, nearly all revenue is collected into one of three main funds: the General Fund, the Public Utility Fund and the Debt Service Fund. The following pie chart shows the City's revenues by source and the percentage of total revenues each source represents.

### 2013 Revenues by Source (\$30,476,041 Total)



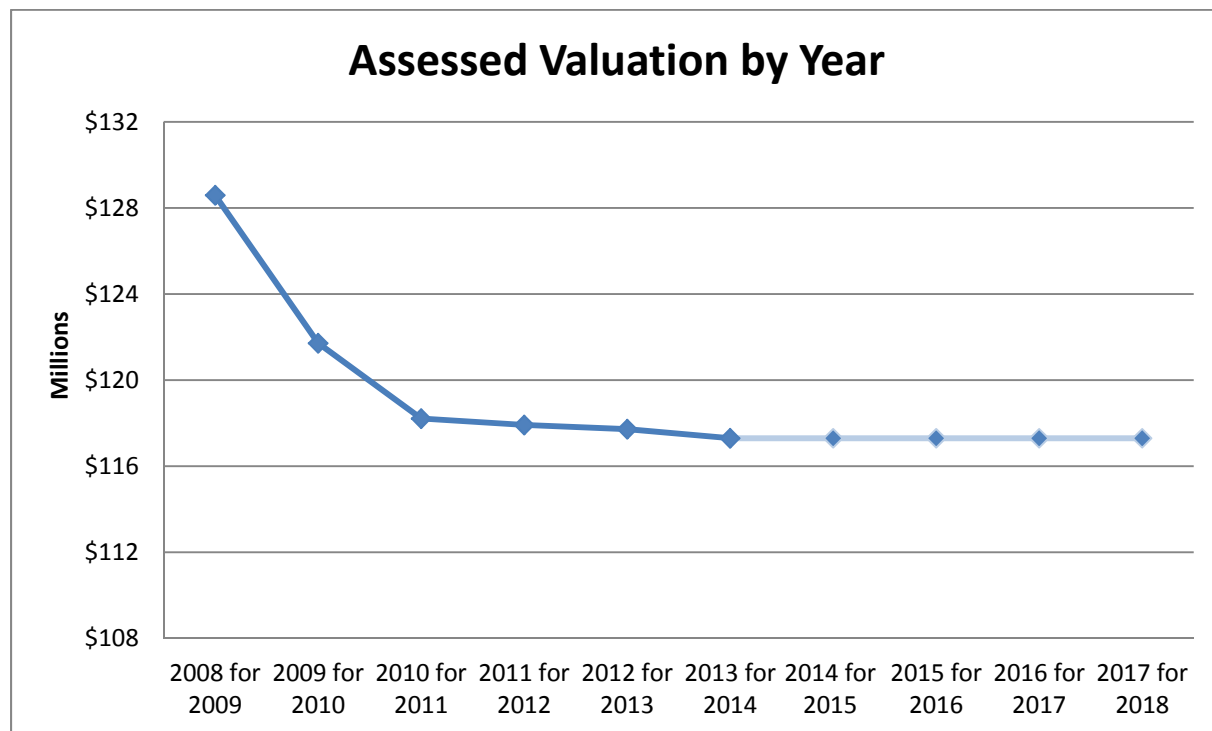
## General Fund

Of the many sources of revenue the General Fund has, the four major sources are: Property Tax, Sales Tax, Franchise Tax and Public Utility Transfers.

### **Property Tax:**

The property tax is an ad valorem tax, meaning it is based on the value of real estate or personal property owned by an individual or company. There are two components for calculating property taxes: property valuations and the mill rate. The City determines the level of service for the upcoming year and sets the property tax rate at an amount which will pay for those services.

The assessed valuations peaked in 2008 with a significantly higher estimate for 2009 than was realized. Beginning in 2009, valuations driving property tax collections experienced a significant decrease through 2010. Assessed valuations have continued to drop (at a slower rate) even with predictions of economic recovery. Since the housing crises, lending practices have tightened, housing prices have plummeted, the economy has had a slight recovery, and unemployment has decreased slightly. However, there are no indications that property values will increase in Crawford County for the next few years, so estimates include a flat valuation rate through 2018. The graph below shows the anticipated trend in assessed valuations.

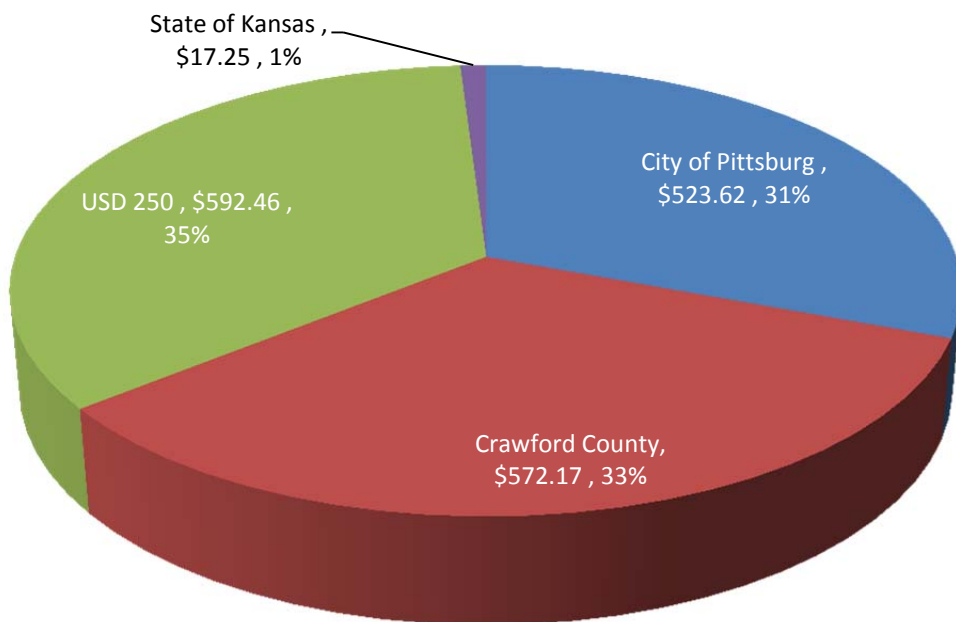


During the time when the valuations plummeted, the mill rate for the City remained constant and was not increased to compensate for the reduction in property values. In 2014, one mill in the City of Pittsburg will generate approximately \$117,495. While the amount of property taxes levied decreased each year since 2009 (see chart below), the projection for 2013 shows a three percent increase over 2012. This is the result of lowering the debt service mill by one and moving it to support general operations.

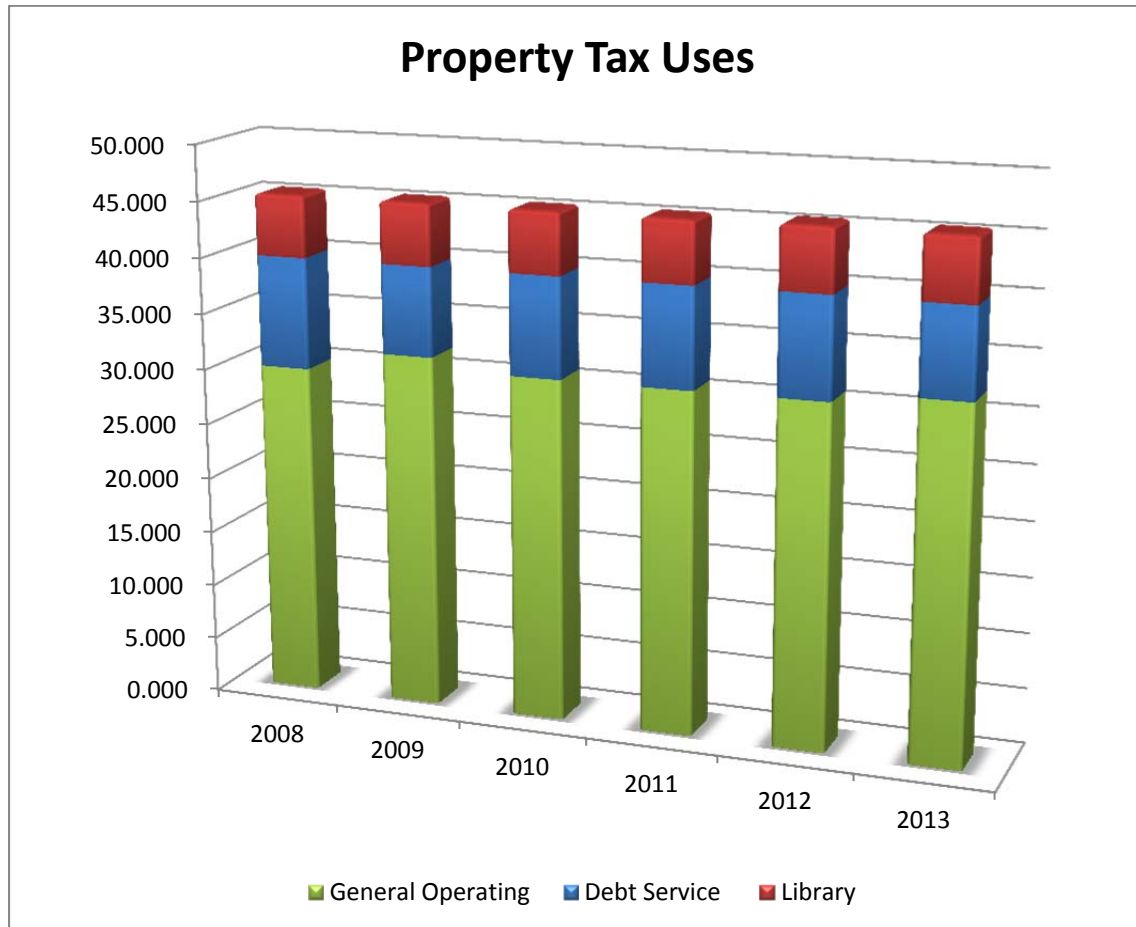
Valued for	Net Valuation	General Fund Mill Rate	Tax Dollars Collected
<b>2009</b>	\$ 128,592,500	31.916	3,909,281
<b>2010</b>	\$ 121,717,189	30.899	3,512,698
<b>2011</b>	\$ 118,213,825	30.907	3,459,433
<b>2012</b>	\$ 117,919,158	30.956	3,481,736
<b>2013</b>	\$ 117,721,546	31.933	3,564,291
<b>2014</b>	\$ 117,495,446	31.880	n/a

The City receives only a portion of the property taxes paid by residents. The State of Kansas, Crawford County and the school district (U.S.D. 250) also assess taxes on property. The pie chart below shows an example of annual property taxes for a \$100,000 home. A one mill increase on a \$100,000 house would equal \$11.50.

### Property Tax on a \$100,000 Residence



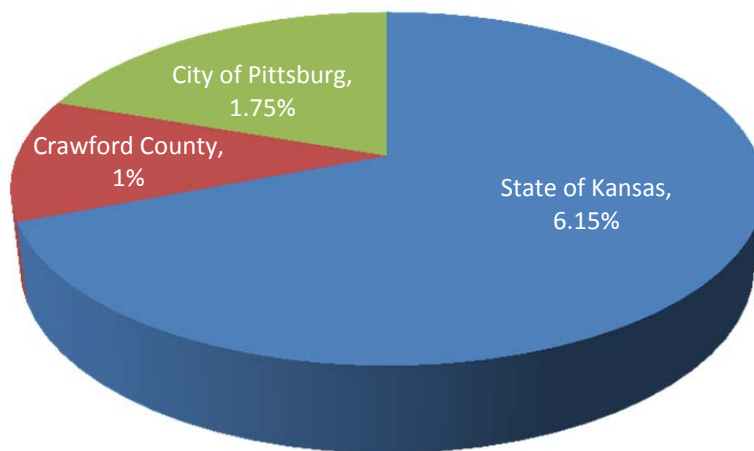
The following graph shows the ways the City uses the property taxes levied:



### **Sales Tax:**

Property taxes represent the second highest revenue source for the City of Pittsburg, second only to sales taxes. However, while the property taxes are unrestricted in use, the sales taxes are restricted. The following chart shows the allocation of the total sales tax rate in the Pittsburg City Limits:

### **Overall Sales Tax Rate - 8.9%**



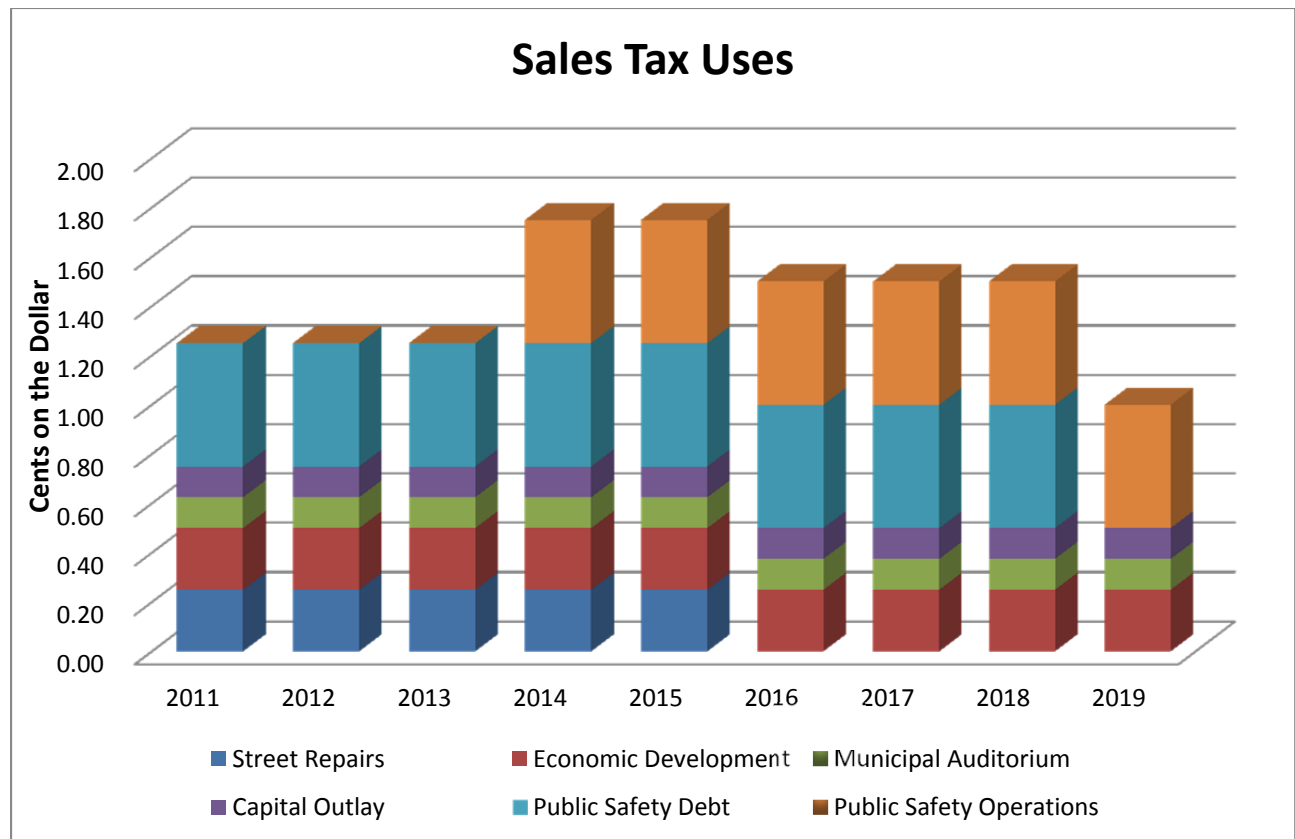


As shown above, the City's portion of the sales tax rate is 1.75 cents and is restricted as follows:

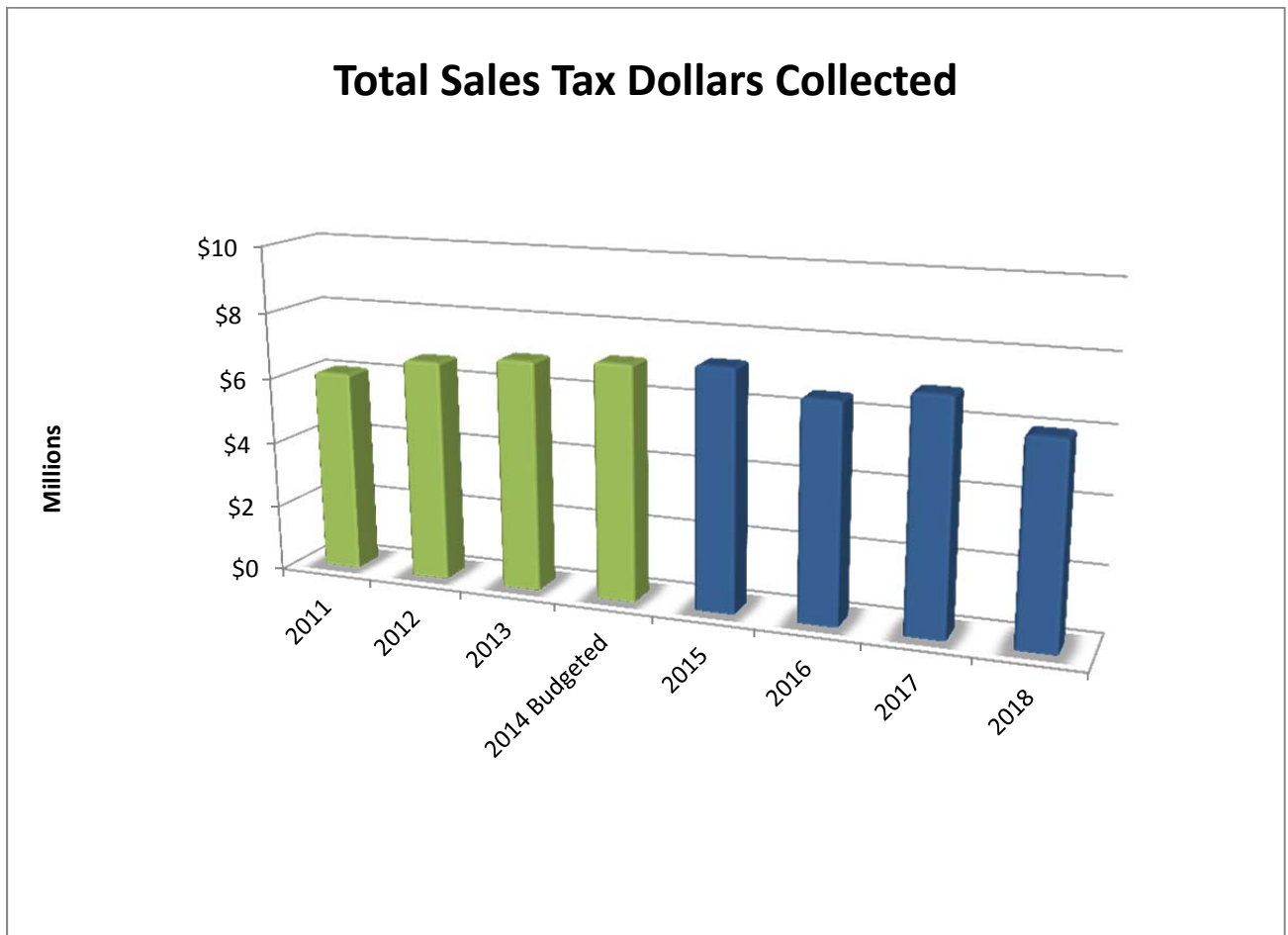
Sales Taxes In Pittsburg		
<u>Purpose</u>	<u>Rate</u>	<u>End Date</u>
Street Repairs	.25	2016
Economic Development	.25	Ongoing
Municipal Auditorium	.125	Ongoing
Capital Outlay	.125	Ongoing
Public Safety Debt	.50	2018
Public Safety Operations	.50	2023
<b>TOTAL</b>	<b>1.75</b>	

There are six programs funded by dedicated sales taxes in Pittsburg. Three have renewal or end dates. The sales tax for street repair was authorized for five years and the Public Safety Debt sales tax is only authorized until the bonds are retired. A sales tax to support public safety operations was recently approved and expires in ten years. The quarter-cent for economic development and the quarter-cent which evenly supports municipal auditorium and capital outlay do not expire.

The graph below reflects the sunset of the quarter cent street paving sales tax after the first quarter of 2016, the retirement of the half cent Public Safety Debt in 2018, and a 2% increase in sales tax collections from 2014 through 2018.



Sales tax revenues dropped from \$5.7 million in 2008 to \$5.3 million in 2010. Since then sales tax revenues have steadily increased. The sales tax revenues for 2015 through 2018 estimates include a 2% increase per year.

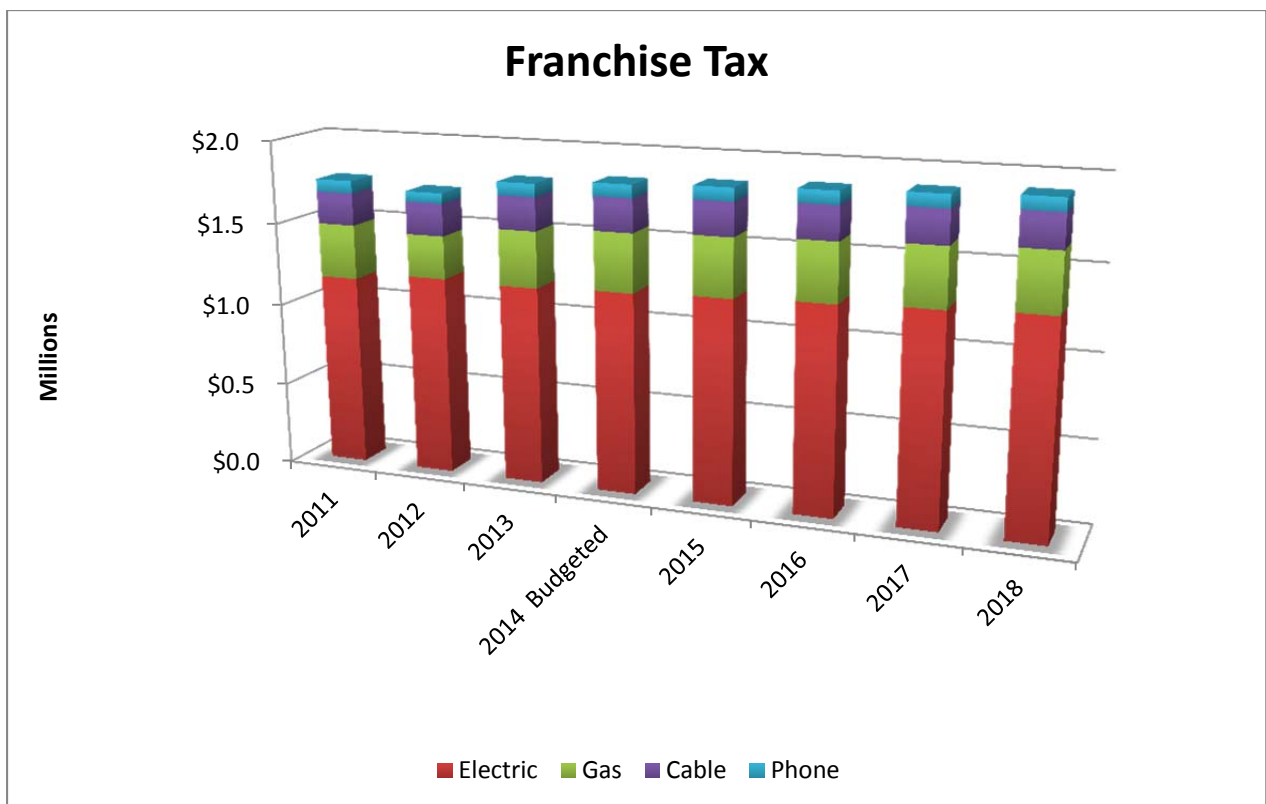


### Franchise Taxes:

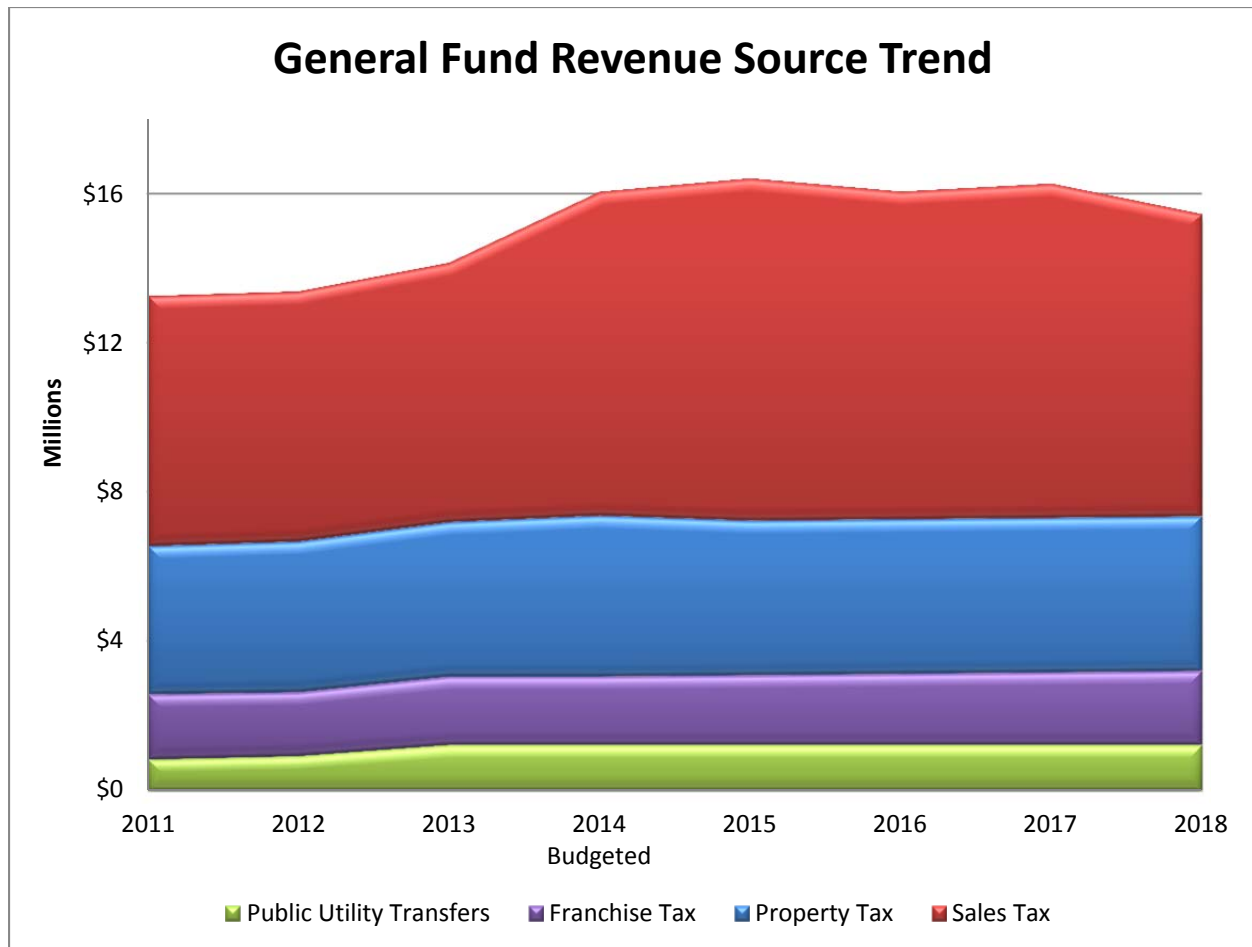
Franchise taxes are the general governments' third largest revenue source; and the second largest unrestricted revenue-second only to property taxes. Franchise taxes for the City include:

- Electric
- Gas
- Cable
- Telephone

Franchise taxes are not consistent, but, their unpredictability is based more on climatic changes and on the commodities market instead of housing and the economy. The electric and gas franchise taxes are specifically driven by climate and commodities. Technology has reduced the dependence on land-line telephones, so that portion of franchise taxes is declining. In addition, the Cox Cable Franchise agreement is up for renewal in 2014. Therefore, the City anticipates a 1.5% increase in only the electric portion of the franchise taxes, as shown below.



The following graph depicts how the City's major source of general fund revenue has shifted from property taxes to sales taxes.

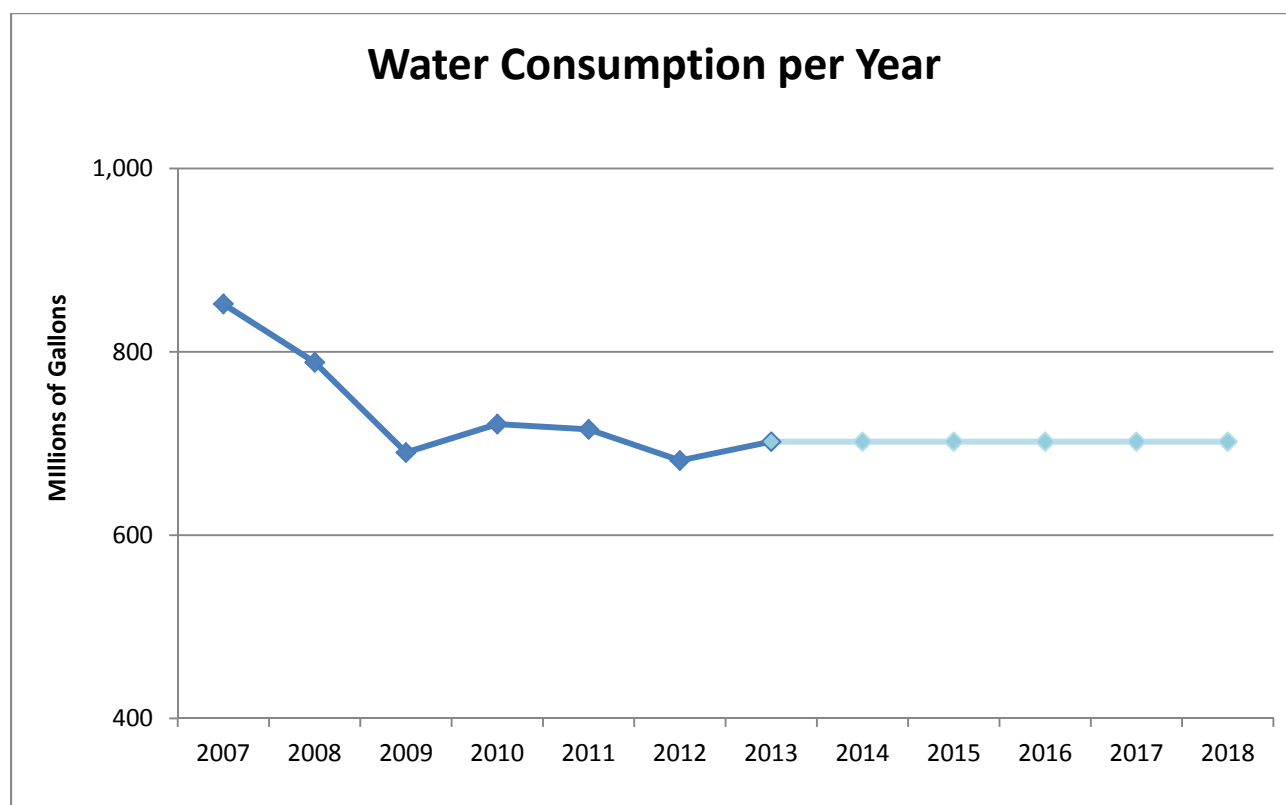


✚ **Other types of Revenues:** The City receives other types of revenues, as well as the ones mentioned above; however, the total is insignificant compared to property taxes, sales taxes, and franchise fees.

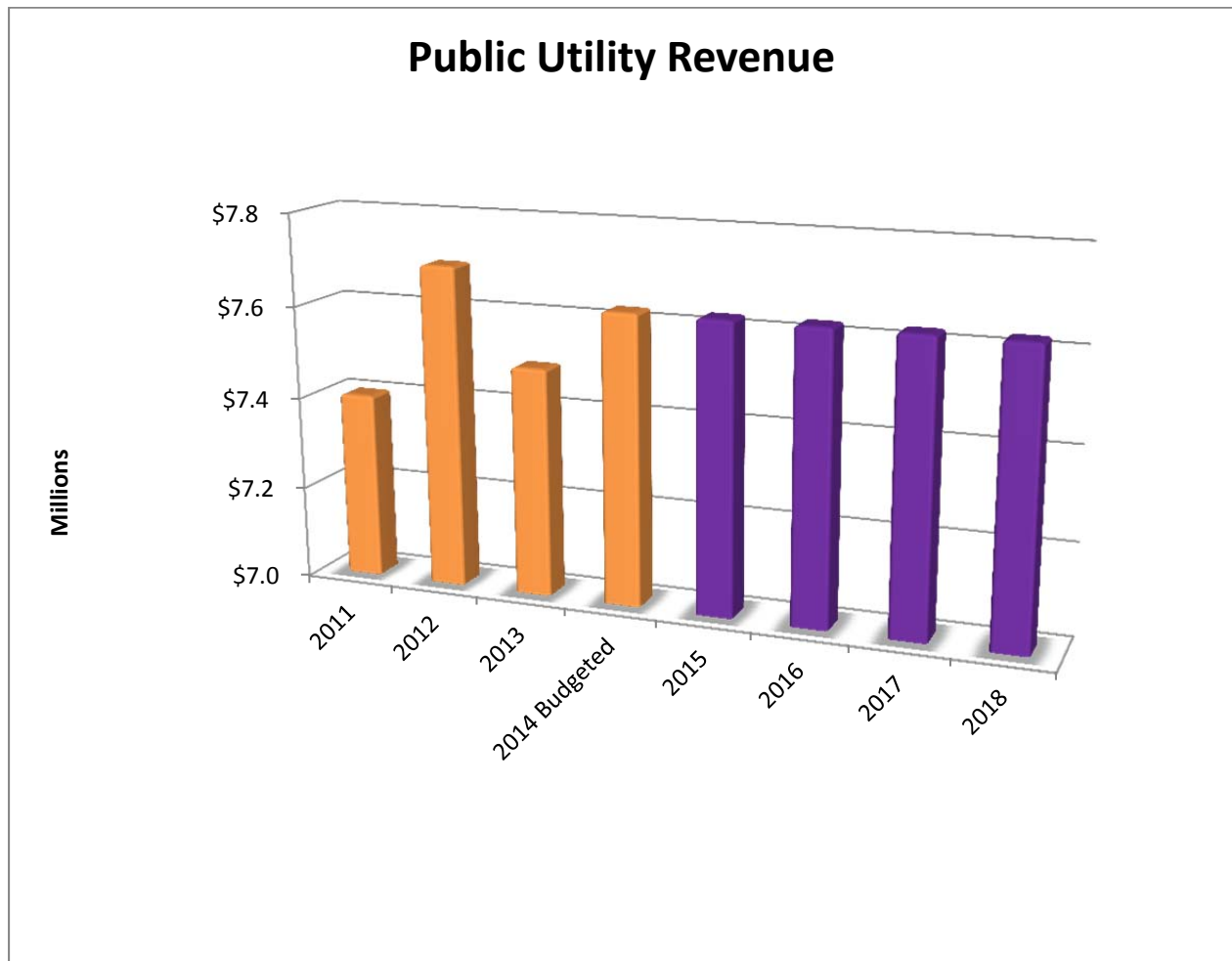
- **Intergovernmental Revenues**
- **Investment Income**
- **Fines and Fees**
- **User fees**
- **Licenses and permits**
- **Miscellaneous revenues**

### Public Utilities:

The primary revenue source for public utility activities is user fees. In the case of water and wastewater, the levels of usage are volatile and based on climatic conditions, as well as types of consumer base. If the season is mild and wet, water use is lower than during high heat and drought conditions. The large drop in water consumption between 2007 and 2009 is due in large part to the closure of a major manufacturer that was the City's primary water consumer. The increase in consumption for 2010 and 2011 results from extreme weather conditions those years. The graph below shows no estimated increase in water consumption for 2015 through 2018, since we do not know what climatic events or economic development will occur to impact the usage.

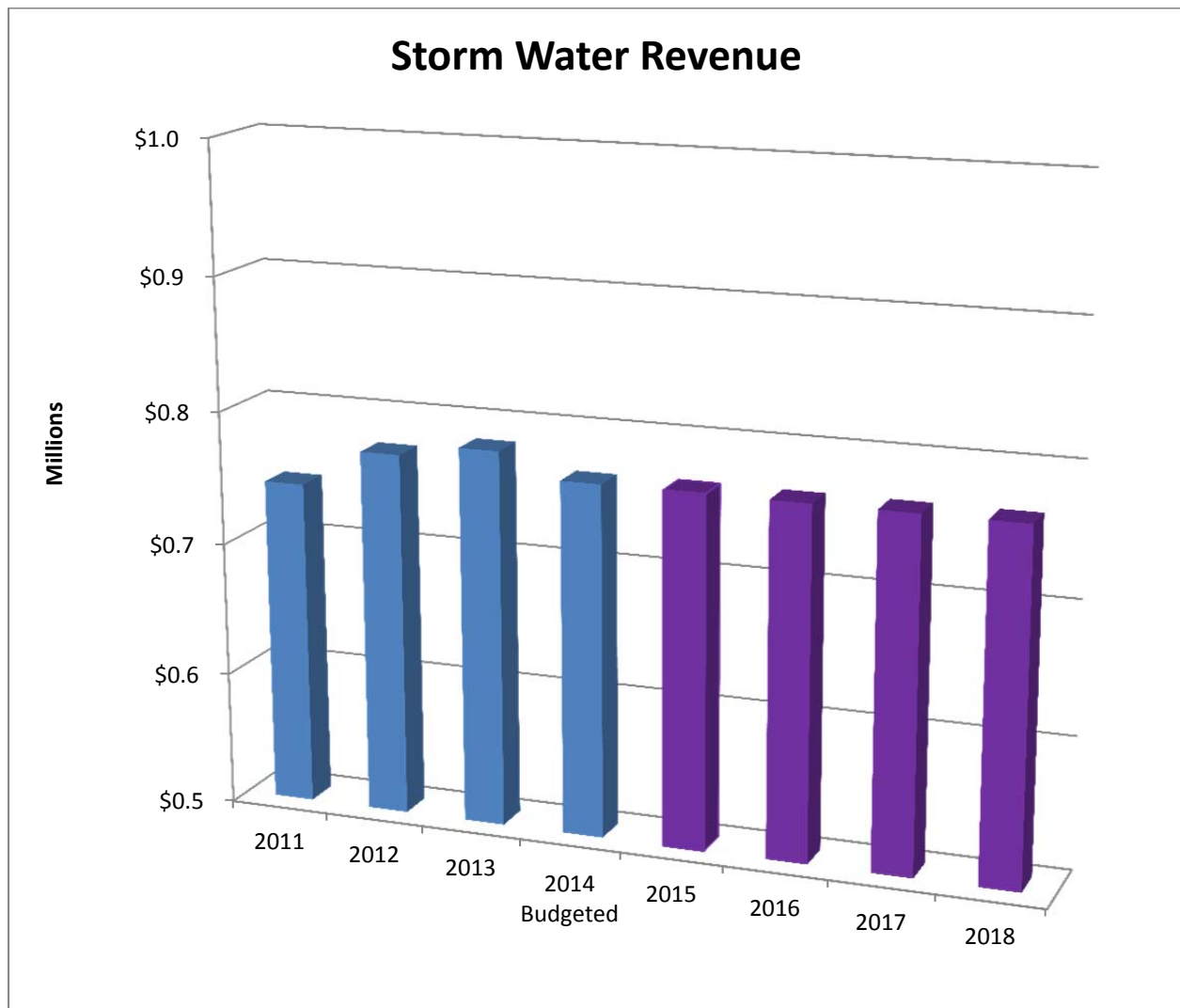


Other issues having an impact on water revenues include water loss, whether through aged meters or unidentified leaks, and rate changes. The last rate increase was effective January 1, 2012.



## Storm Water:

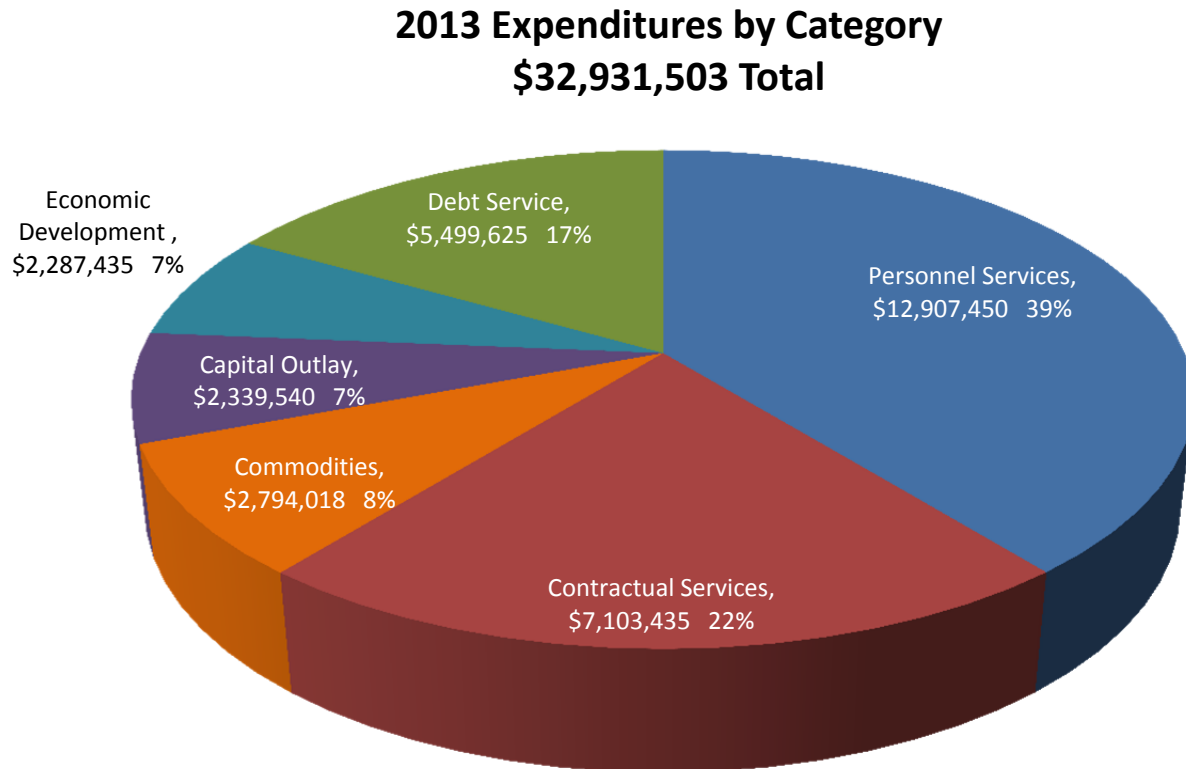
Storm Water revenues are not tied to climatic conditions but are based on average impervious area. In November 2011, the City passed a resolution which established the definition of the average impervious area unit and established a rate per unit. The last rate increase was effective January 1<sup>st</sup>, 2012. This change explains the increase in revenues for 2012. The increase in 2013 includes a transfer from the Public Utility Fund.





## EXPENDITURES

With the reductions in revenues, the City is redirecting its financial focus to performance- based initiatives and is budgeting expenditures accordingly in order to accomplish goals. The following chart shows the expenditures by category for 2013.

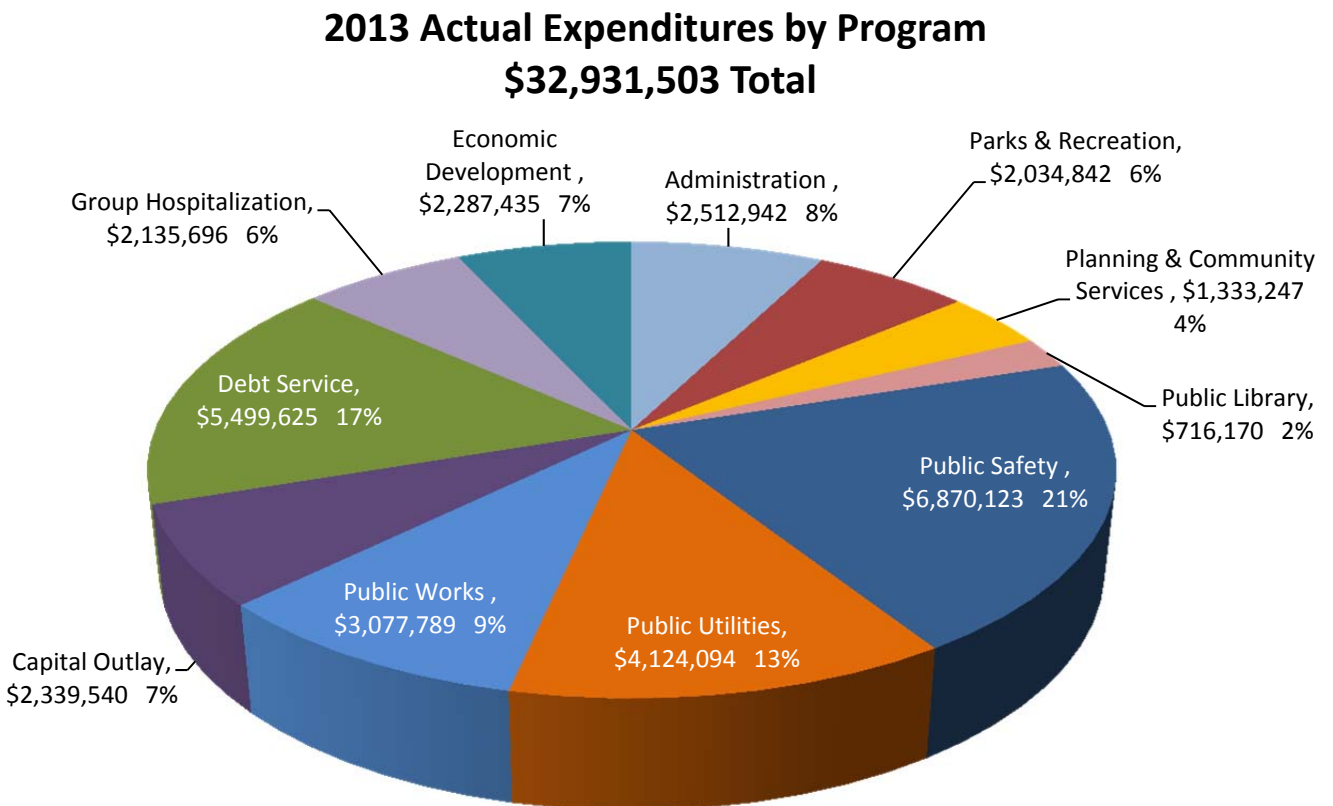


Personnel expenditures, as is the case with most entities, represent the majority of the City's expenditures. Personnel costs include salaries and benefits. The 2014 Budget does not include Cost of Living Adjustments (COLAs), but does include anticipated increases for the Kansas Public Employees Retirements System (KPERs), Kansas Police and Fire (KP&F) retirement, as well as increases for health insurance and worker's compensation. Recently KPERs announced significant unfunded actuarial liabilities which existed for several years. The Kansas Legislature approved a plan to increase employer contributions to compensate for the shortfall. This forecast includes the anticipated increase to be passed on to employers.

Contractual services includes a variety of expenses including but not limited to property and liability insurance, group medical insurance, software license agreements, utility costs, and lease payments for certain equipment. As these items are tied to the cost of living, consistent growth is inevitable and since this represents nearly one-fifth of the General Fund, the impact on services could be significant.

Debt service and transfers represent the next highest expenditure categories. Most of the transfers are from the General Fund to other funds in support of specific activities and for debt repayment. The public utility funds also make transfers into the General Fund and Debt Service Fund.

Another useful way to view the City's expenditures is by program. The 2013 expenditures by program are shown below. The Public Safety Program holds the largest percentage of expenditures. The second largest expenditures are for Debt Service and Public Utilities, respectively.



## **Group Hospitalization**

One of the benefits the City provides is health care coverage to both active employees and their dependents and age/service-eligible retired employees who have not reached the Medicare eligibility age of 65, and their dependents.

The city's health care plan is a self-funded plan paid for by annual appropriations and participating employees' contributions to the plan. Self-funded plans are often referred to as "pay as you go." This is because the claims are paid as they are incurred rather than paying premiums. Any balance that is unused stays in the fund to help offset future costs.

While being self-funded has the advantage of paying for only what is used, health care costs still increase annually. Based on the city's historical costs for the past seven years, the average increase in health care cost has been 8.84%. During 2014 some changes were made to the plan, which may reduce the 8.84% increase to 5%. The long-term financial plan annual calculations for 2015 through 2018 were based on the 5% average.

Since 2007, annual expenses have fluctuated and have been higher than the revenues generated for four of those seven years. Fortunately, there were reserves available to offset the shortfall. At the current rate of revenues to expenditures, there will be no reserves left in this fund by 2015. The following options are available to correct this:

- Change plan/administrators
- Increase employer/employee contributions
- Increase plan deductibles
- Combination of all three of the above options

## **Capital Improvements**

Capital expenditures are resources used to acquire, maintain, repair, replace, or upgrade fixed assets. Fixed assets are typically those assets with a life span exceeding a normal business cycle and whose cost exceeds a minimum dollar threshold established by management.

These assets are used to provide services to the public and during the course of their lifetime will require maintenance to keep them operating safely and efficiently. The performance and continued use of assets is essential to the health, safety, economic development, and quality of life for the public.

Budgetary pressures often cause maintenance to be delayed due to lack of resources. This is referred to as deferred maintenance. Prolonged deferred maintenance results in higher costs, asset failure, and health and safety issues. Therefore, in order to adequately address these issues, a capital improvement plan is essential.

Currently, the City's fixed assets have a net value in excess of \$100 million dollars. It is estimated that the city should spend about 5% of the value of assets, annually, on maintenance. This equates to approximately \$5 million dollars each year.

The City has identified in excess of \$56 million dollars of upgrades, maintenance or replacements necessary over the course of the next few years. Effective financial management includes a capital management plan that will address these needs. The capital Improvement program located in the supplemental information section summarizes the estimated costs of repairs, maintenance, and replacements for 2014 through 2018, by department and asset type.

## **DEBT SERVICE**

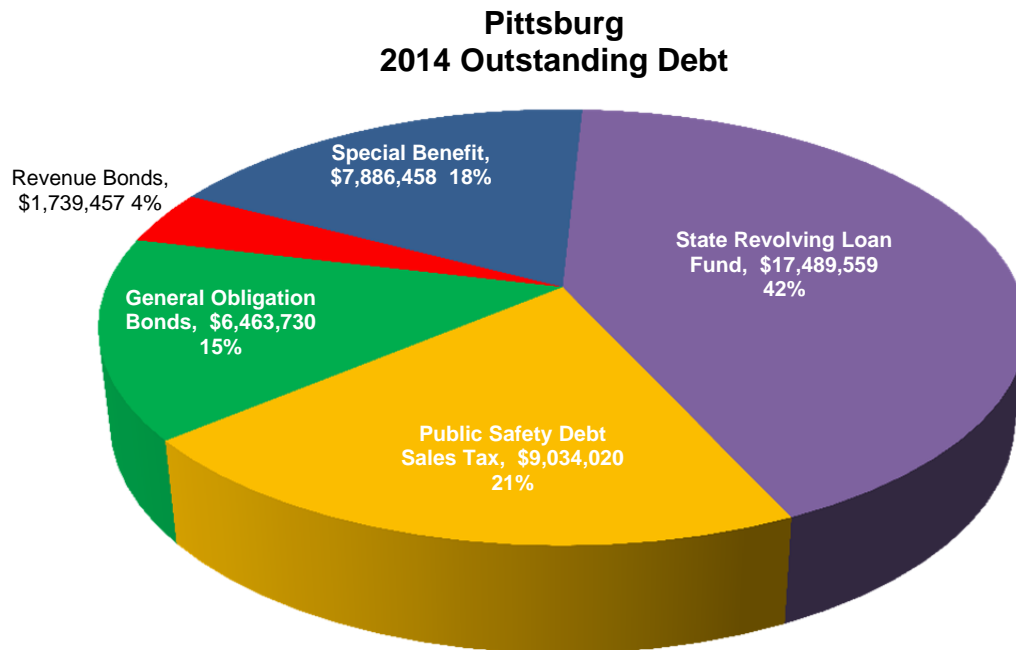
Effective financial management includes analyzing several funding mechanisms to determine what option is the most beneficial to the City. In some cases, issuing debt is the best available option. The City of Pittsburg traditionally uses debt for equipment and capital improvements which cost too much to pay from the operating budget. The financial plan for the City includes debt payments for current obligations and forecasted payments associated with refinancing temporary notes issued in 2013. Those additional payments are anticipated to begin in 2015.

The revenues for making the debt payments are derived from the following sources based upon the nature of the improvement and the type of debt that has been issued:

- Property taxes
- Charges for Services
- Special Assessments
- Investment Income
- Transfers
- Other

## Types of Debt

The City of Pittsburg uses several types of debt to pay for capital improvements and expensive equipment. The graph below shows the type of debt and the percentage each is of the City's total debt.



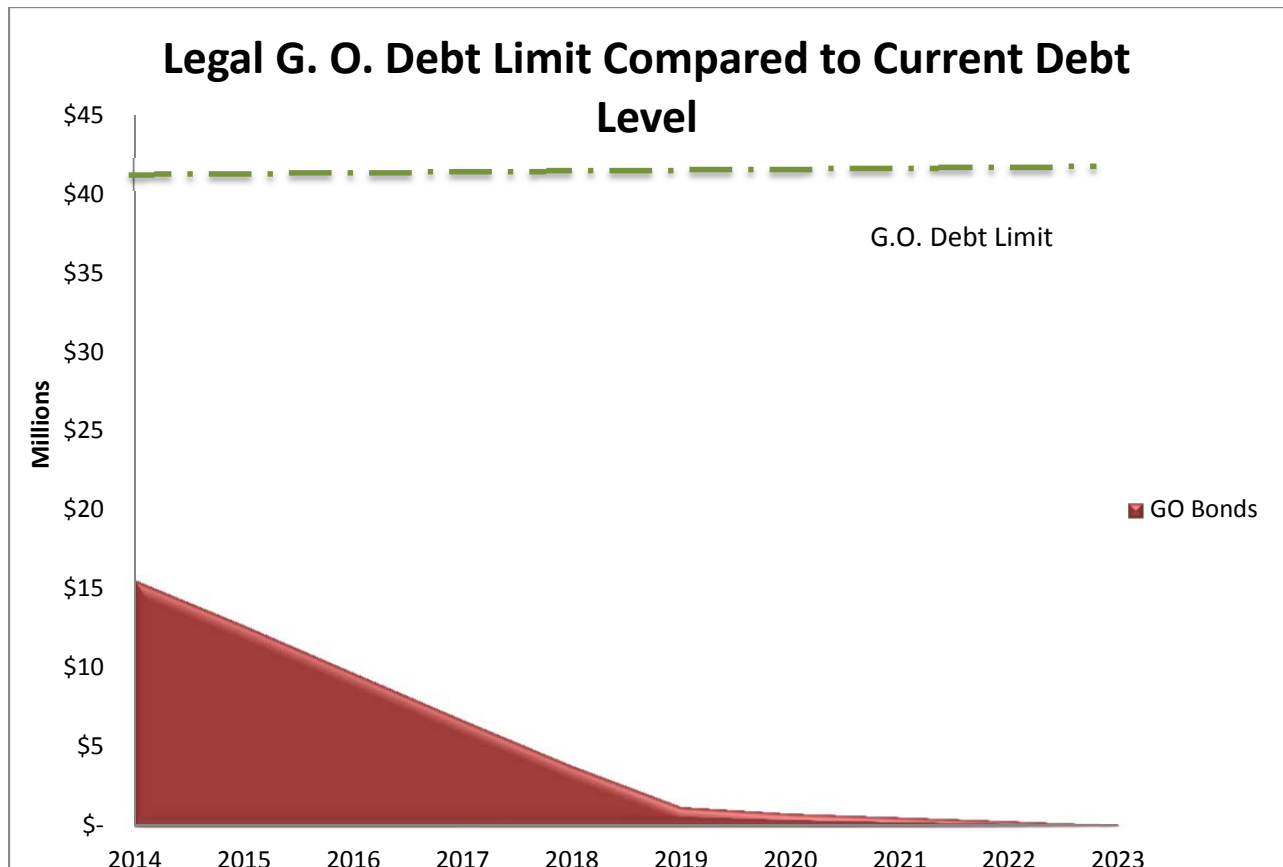
Effective debt management requires monitoring debt levels to ensure the soundness of the City's financial position and continued credit worthiness. The City uses the following measurement tools to manage its debt levels:

## Fiscal Year 2014

Net direct bonded debt:

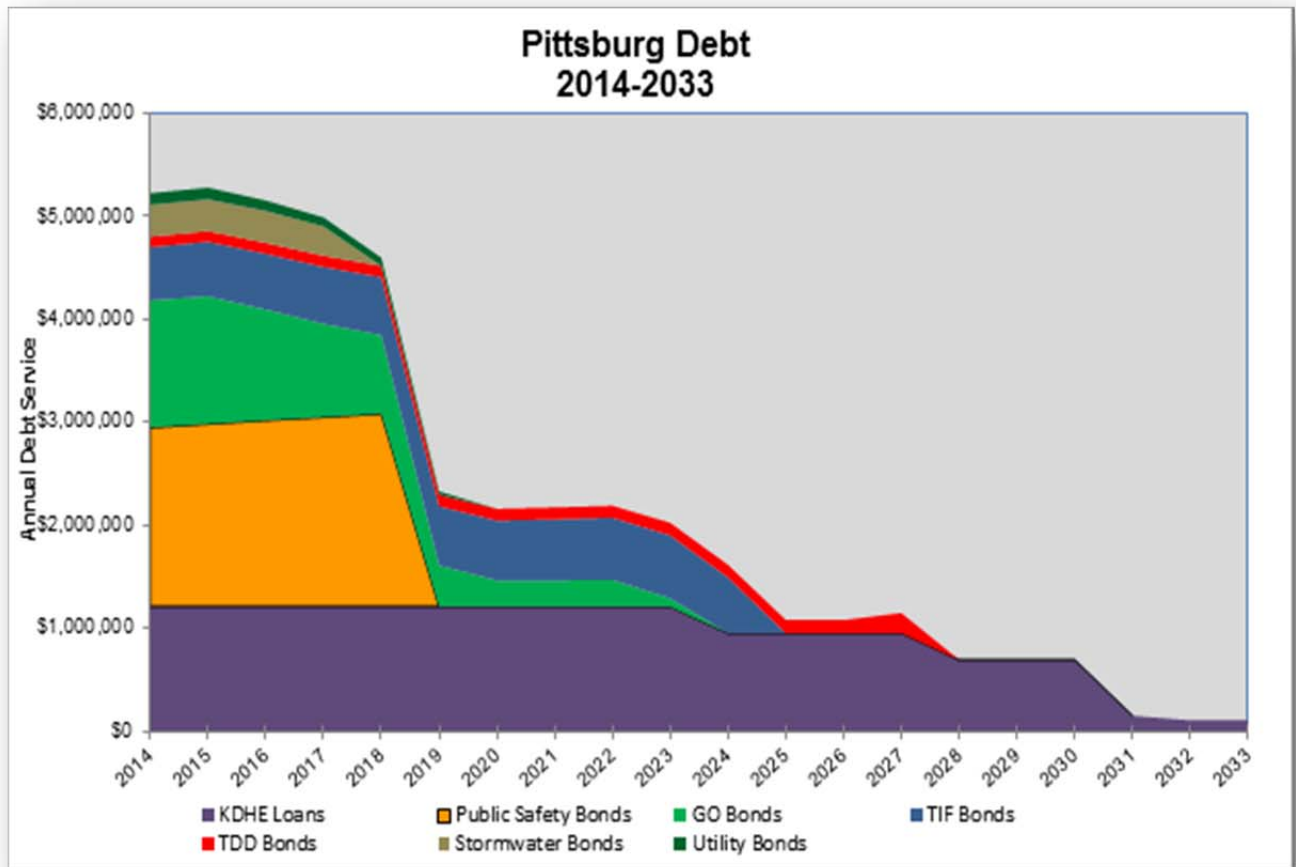
Statutory requirements for Tax Supported Debt (less than)	30%
City's Tax Supported debt (as a percentage of Assessed Valuation)	6.4%
General Obligation Debt per Capita	\$ 795
Mills	8 mills

The following graph shows the difference between the City's current total outstanding G O Debt compared to what is allowed according to state statutes. The dark red indicates the City's current level of G O Debt and the green line indicates the legal limits (the 30% of assessed value mentioned above):



### Cumulative Debt:

The following graph depicts the City's total annual debt by type and the year the bonds are scheduled to be retired. As of 2019, the Public Safety Bonds, Storm Water Bonds, and the majority of the G.O. Bonds are scheduled to be retired.





## RESERVES

Reserves are the cornerstone of financial stability and flexibility, providing an organization options with which to respond to unforeseen risks. The most challenging issue regarding reserves is the balance between enough and too much. While there is no specific right or wrong answer, there are analytical tools that can determine what an appropriate level is for each organization. Several risk factors to be considered are:

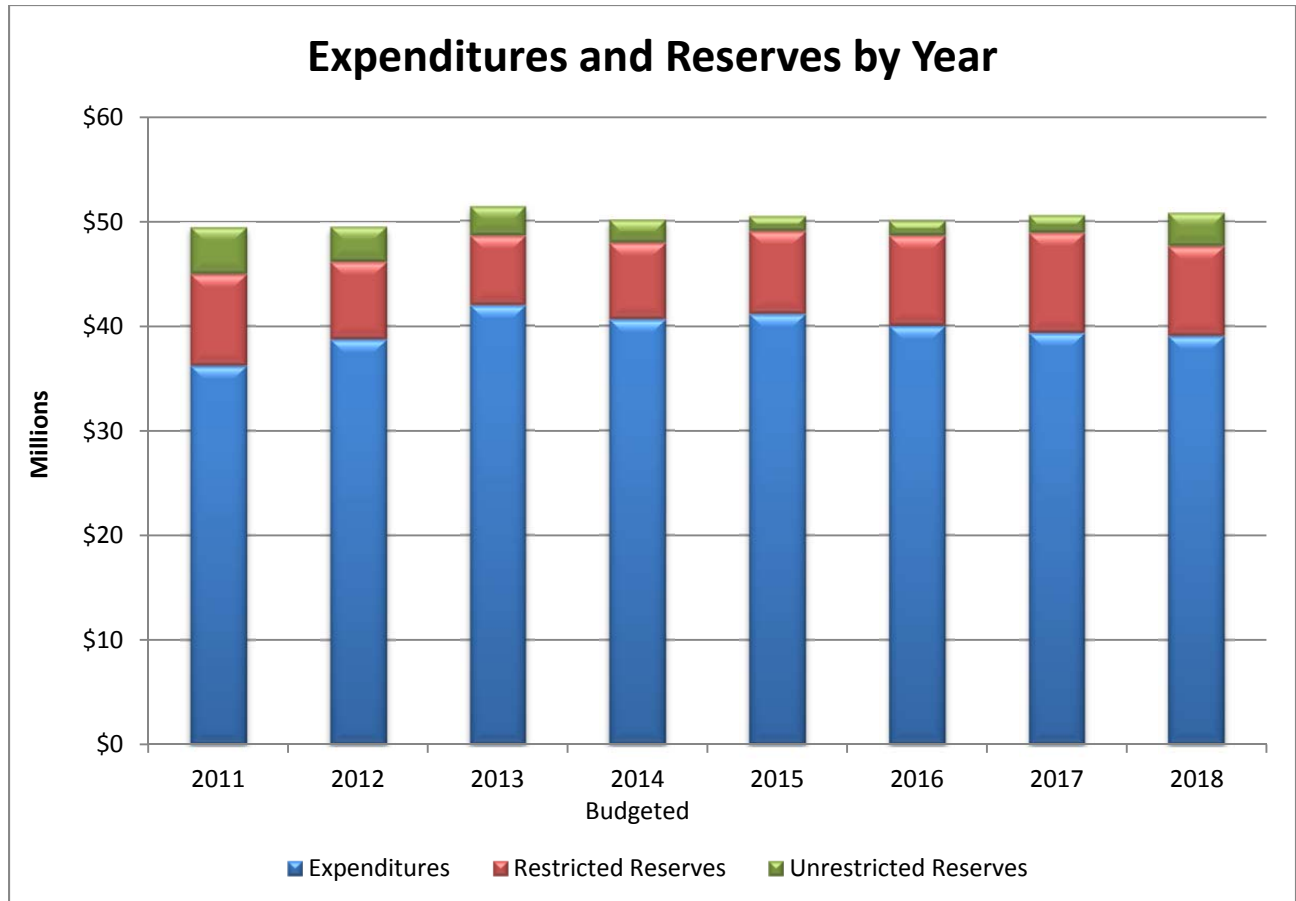
- Revenue volatility
- Infrastructure condition
- Extreme events such as weather
- External Factors

The Government Finance Officers Association (GFOA) recommends adequate reserves are 16% of expenditures for governmental funds and two months of expenditures for enterprise funds. The City has determined that it should maintain the equivalent of two months of expenditures as a minimum reserve level.

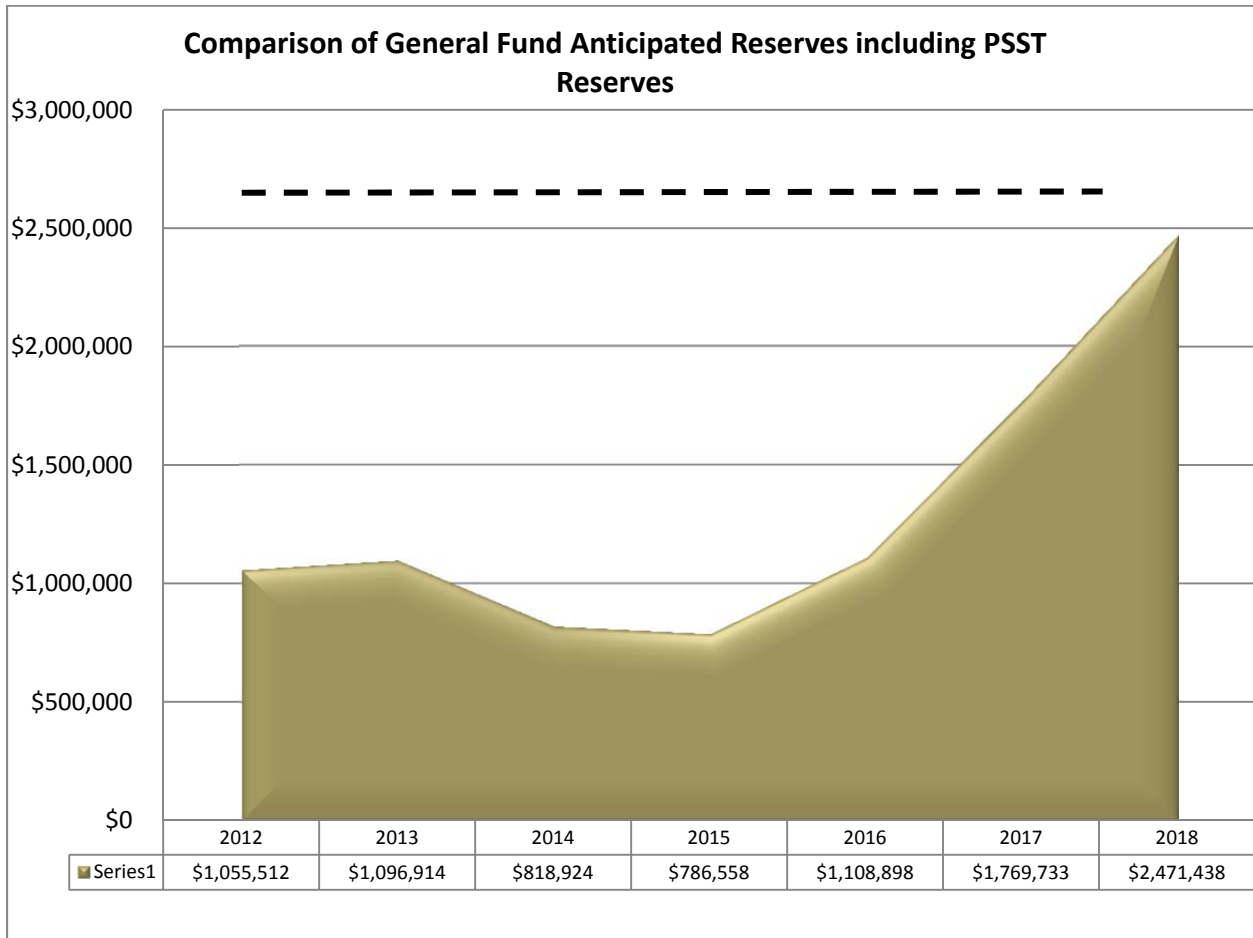
During the economic downturn, some minor measures were taken to offset the decrease in property tax revenues including staffing reductions through attrition and some reductions of expenditures, however, reserves were used most often to pay for programs and services.

As a result of minimal growth in property tax collections, sales taxes, fines and fees, and no growth in other revenue sources, reserves have significantly declined. It will be difficult to protect our current reserves and it will be impossible to replenish our reserves without adjusting our spending and revenue picture.

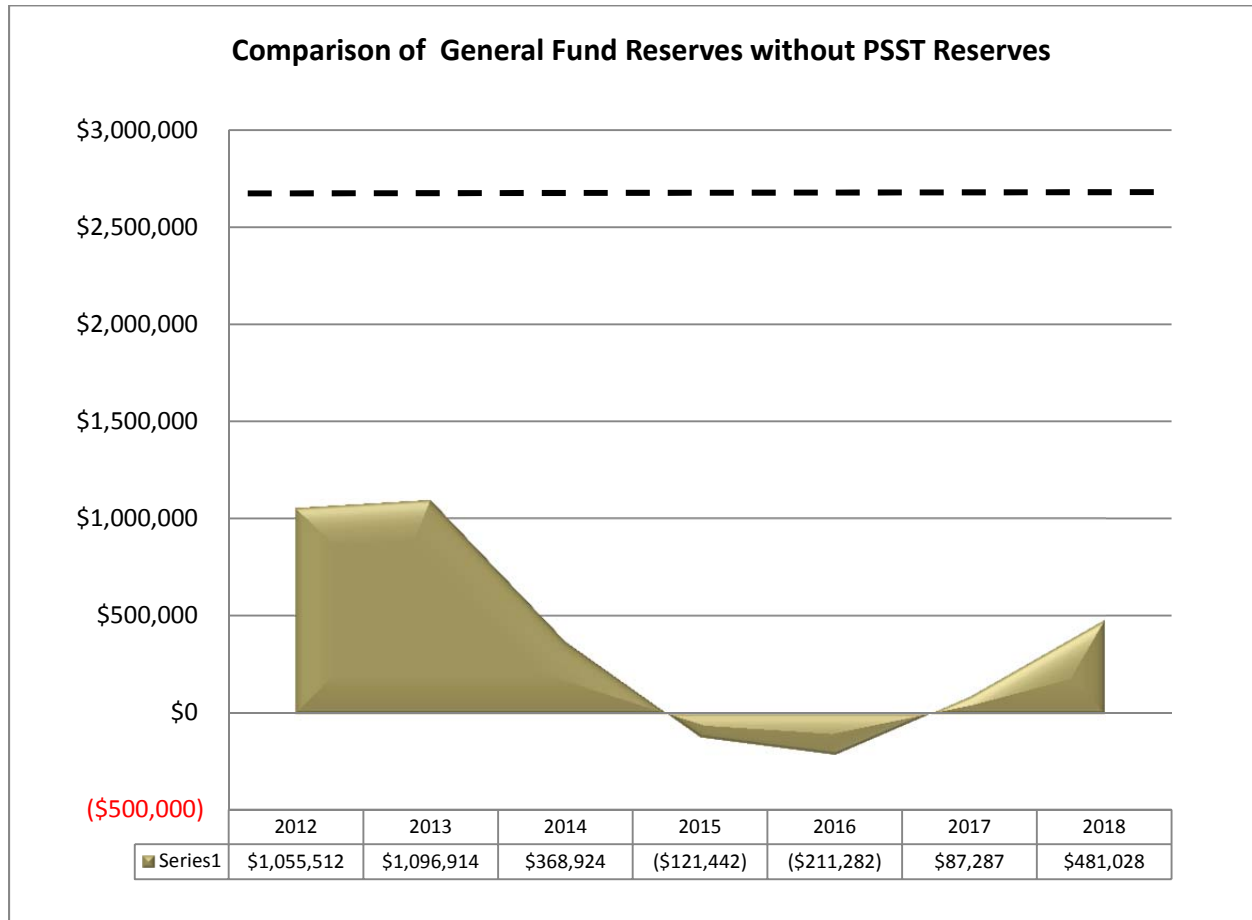
The Chart below shows the impact of changes in expenditures on restricted and unrestricted reserves.



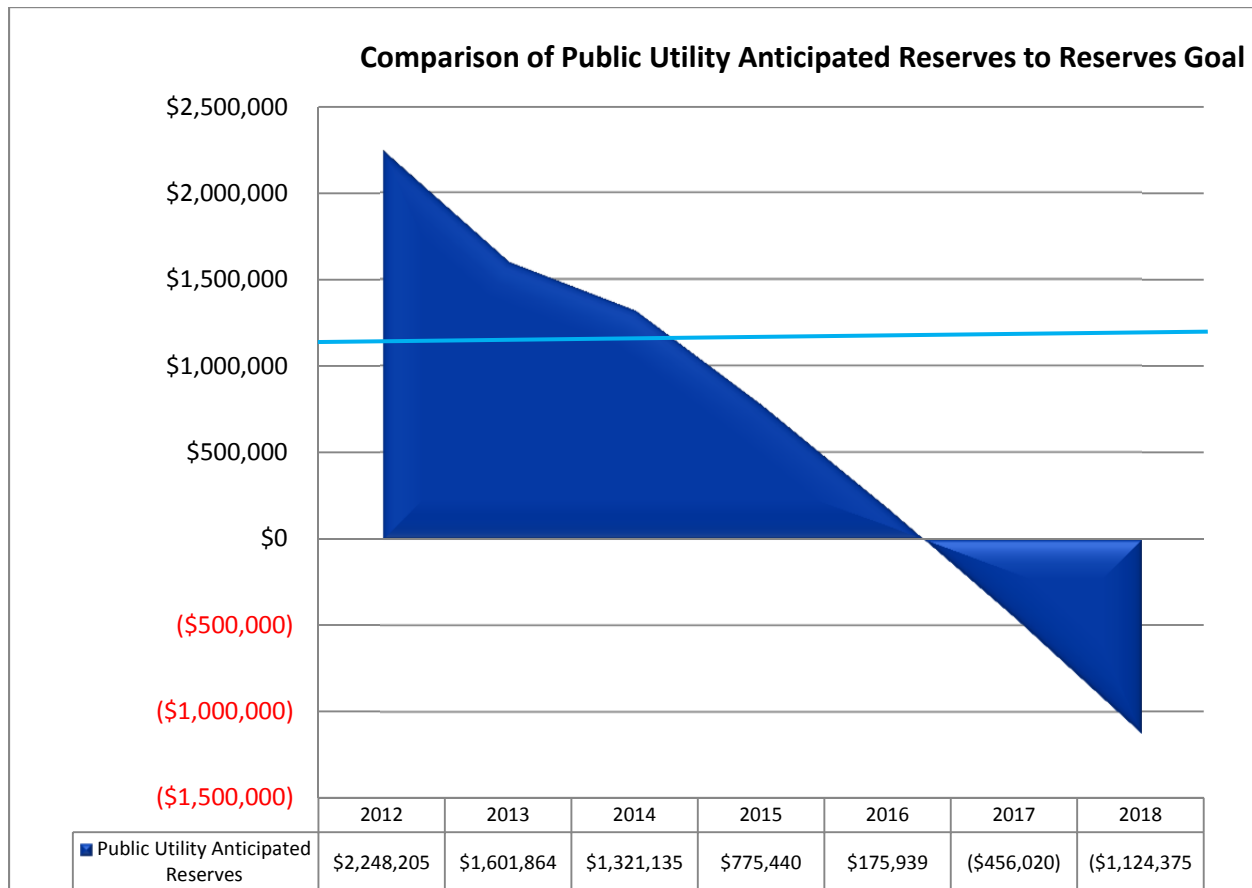
By the end of 2014, the reserves for General Fund are estimated to be \$818,924, as shown below. This amount is significantly under the baseline amount established in the Budgetary Reserve Policy. If the City were able to maintain the minimum two month reserve goal, the 2014 reserves should be \$2,860,532, a shortfall of over \$2,000,000. And while the reserve level appears to increase beginning 2016 through 2018, those reserves come from the Public Safety Operations sales tax and the Public Safety Debt Sales Tax and are, therefore, not available for general operations.



The following graph shows the general fund reserves level *without* the Public Safety Operations reserves:



By the end of 2014, the reserves for Public Utility are estimated to be \$1,078,378. While this amount is slightly under the reserve goal for 2014, the downward trend of reserve levels continues. By 2017, the public utility reserves will be depleted without some remedial action, as shown below.



## **SUMMATION AND RECOMMENDATION:**

Fortunately, the City of Pittsburg had reserves to rely on during the worst of the economic downturn; however, those reserves have declined because they have been used to balance the budget. Current decisions and plans will have a direct impact on the financial stability and the ability of the City to thrive throughout future financial challenges. The purpose of this document is to outline the current financial position and provide insight to some of the issues that the City faces in the near future.

As mentioned earlier, external factors are those that the city has very little control over and yet those factors have a significant impact on our financial position. Some of those factors are property valuations, extreme or unusual weather, intergovernmental funding source reductions, health insurance costs, property and liability insurance costs, retirement rate changes, and other consumer pricing increases.

Deferring maintenance on city infrastructure and other fixed assets is both costly and inefficient. Providing service to the citizens efficiently and effectively requires that we devote resources to maintaining and/or replacing those assets.

As mentioned previously, reserves have significantly declined. It will be difficult to protect our current reserves and it will be impossible to replenish our reserves without adjusting our spending and revenue picture.

To ensure our future financial stability we must consider:

- ✓ Increasing revenues incrementally
- ✓ Monitoring and controlling expenditures
- ✓ Building reserves
- ✓ Practicing long term planning
- ✓ Adopting and following written policies
- ✓ Making data driven decisions

Specifically we recommend:

1. Increasing the mill rate
  - a. In the 2015 Budget by 4.0 mills
  - b. In the 2016 Budget by 3.0 mills
  - c. In the 2017 Budget by 1.0 mill

2. Increasing utility revenues by 3% a year for each of the next five years
3. Adopting the following long term plans
  - a. Five Year Capital Improvements Plan
  - b. Five Year Equipment Replacement Plan
  - c. Five Year Financial Forecast
4. Adopting the following policies to guide our daily practices:
  - a. Debt Policy
  - b. Purchasing Policy
  - c. Revenue Policy
  - d. Reserve Policy
5. Holding the line on expenses by limiting increases to:
  - a. 2.5% salary increase in 2015 and 2.0% in 2017.
  - b. Increase the employer contribution for health insurance by 2% per year to meet the increasing cost for group hospitalization

Changes in our economic condition will affect our projections. We will review our situation every year and adjust our activity appropriately.