City of Buffalo

Department of Audit & Control

Budget Response

2013-2014 Fiscal Year
&
2013-2017 Four Year Financial Plan

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Charter of the City of Buffalo

§ 20-7 Comptroller's Assessment of Accuracy of Revenue and Expenditure Assessments.
[Amended 10-2-2012 by L.L. No. 1-2012, effective 10-2-2012]

"On or before the tenth day of May, the Comptroller shall submit to the council an assessment of the accuracy of the revenue and expenditure estimates of the budget and the four-year financial plan the mayor submits to the council. The comptroller shall opine on the sufficiency of the financial plan and whether it contains sufficient data to support the outcomes projected."

Introduction

Pursuant to the City Charter, and the Comptroller's role as the City's chief fiscal officer, I hereby submit this response to the Mayor's recommended budget for the Fiscal Year 2013-2014, as well as the 2013-2017 Four-Year Financial Plan.

The City of Buffalo is currently in strong financial condition, as evident in our bond ratings with the "Big 3" credit rating agencies, including an A+ from Fitch Ratings, an A1 from Moody's Investor Services, and an A from Standard & Poor's. These ratings, which reflect the City's healthy cash position and recent economic progress, have allowed the Comptroller's office to refinance debt for the City and its school district at lower interest rates. Since April 2012, this effort has yielded savings of more than $62 million by reducing interest payments on our debt.

Reducing the City's debt burden has had a positive impact on fiscal health and our bottom line. So have conservative budgeting practices, setting money aside for emergencies in the Emergency Stabilization, or "Rainy Day," fund, and annually accruing funds for unsettled union contracts.

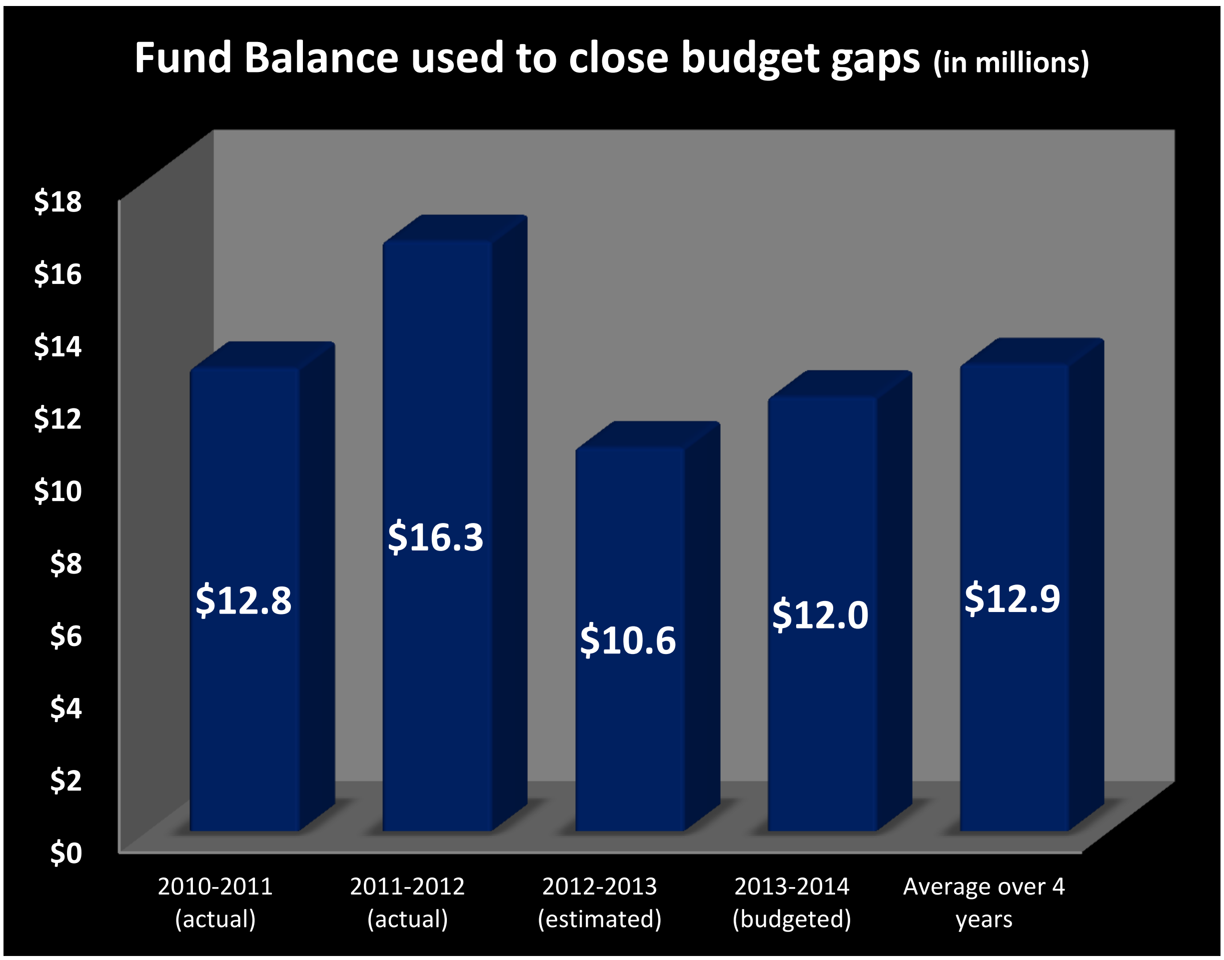
However, decreasing revenues and rising pension and health care costs have made the task of balancing the budget especially difficult. Some of the practices used to close budget gaps could weaken the City's finances and jeopardize its bond rating, especially when relied upon year after year. The most concerning of these practices is the use of fund balance and other one-time revenues, as opposed to finding new recurring sources of revenue to meet the burden of increasing expenditures.

Fund Balance

The mayor's recommended budget uses $12 million in unassigned fund balance to close the budget gap in fiscal year 2013-2014. It will be the fourth consecutive year that reserves will be utilized to balance the budget.

In fiscal year 2010-2011, $12.8 million was used to balance the budget, $16.3 was used in fiscal year 2011-2012, and if the administration's estimate of a $5 million budgetary surplus in fiscal year 2012-2013 is accurate, $10.6 million in fund balance will be needed in the current fiscal year.

The total fund balance used for all four fiscal years, assuming all estimates are accurate, would be $51.7 million, which equates to an average of $12.9 million per year.



The “Big Three” Credit rating agencies – Fitch Ratings, Moody’s and S&P – have repeatedly warned the City about relying on reserves to close budget gaps, especially if the practice becomes a trend.

FitchRatings

“The ability of the city to meet its goals of reducing its reliance upon budgeted reserves and restore structural budgetary balance will be important credit considerations.” – Rating report, April 1, 2013

MOODY’S

“What could make the rating go down: Continued use of reserves beyond what’s currently expected.” – Rating report, April 1, 2013

STANDARD
&POOR’S

“The ongoing use of reserves and one-time revenues for recurring expenditures could pose significant challenges to future budgets.”

– Rating report, April 1, 2013

The rating agencies have made it clear that continued use of reserves could jeopardize the City’s ratings. A potential downgrade by any of the three rating agencies would result in increased interest costs for the City, making it more expensive to borrow funds.

The rating agencies, however, are not the only organizations monitoring the City’s use of fund balance. In January 2013, the Office of the New York State Comptroller implemented the Fiscal Stress Monitoring System, a tool designed to clearly identify those local governments that are moving towards, or are already in, fiscal stress. Buffalo has not yet received its grade, and a significant factor used by the state comptroller in determining fiscal stress is fund balance.

"The level of a local government's year end fund balance can affect its ability to deal with revenue shortfalls and expenditure overruns. A negative or low level of fund balance can affect the local government's ability to provide services at current levels." - Office of the New York State Comptroller, January 2013

While the total fund balance as of the close of last fiscal year is $113 million, the only portion that can be used to balance the budget is the unassigned fund balance, which only has $12.2 million. After the use of $12 million to close the budget gap, and an estimated replenishment of $8.2 million from other sources, the unassigned fund balance will have approximately $8.4 million at the close of the current fiscal year, $4.5 million less than the 4-year average used to balance the budget.

In addition to the use of $12 million from the City's general fund balance, the 2013-2014 budget transfers $4.4 million in reserves from the parking enterprise fund. Monies in the parking fund balance were set aside for long-term capital improvements to parking ramps, not to fix the City's operating budget shortfalls.

One-Time Revenues

As Standard & Poor's noted in the aforementioned quote from its rating report, the use of other one-time revenues for recurring expenditures is also a major concern. The 2013-2014 budget includes the use of $12 million in state aid currently held by the Buffalo Fiscal Stability Authority. Including this appropriation, the City will have used $41.5 million of the $41.7 million in these funds since 2008, eliminating it as a resource in future years.

Another one-time revenue is the use of $4.2 million in proceeds from the Foreign Fire Insurance Tax, representing five years' worth of payments that were being set aside pending ongoing litigation. This is not a recurring revenue source, as it will only generate approximately $300,000 annually in the future.

The budget also includes a $9.6 million transfer from the parking enterprise fund, including the $4.4 million in fund balance previously mentioned, as well as a $5.2 million in revenue from an operating surplus. This will be the third consecutive year surplus revenue from the parking fund has been "swept" into to the general fund to subsidize other operations.

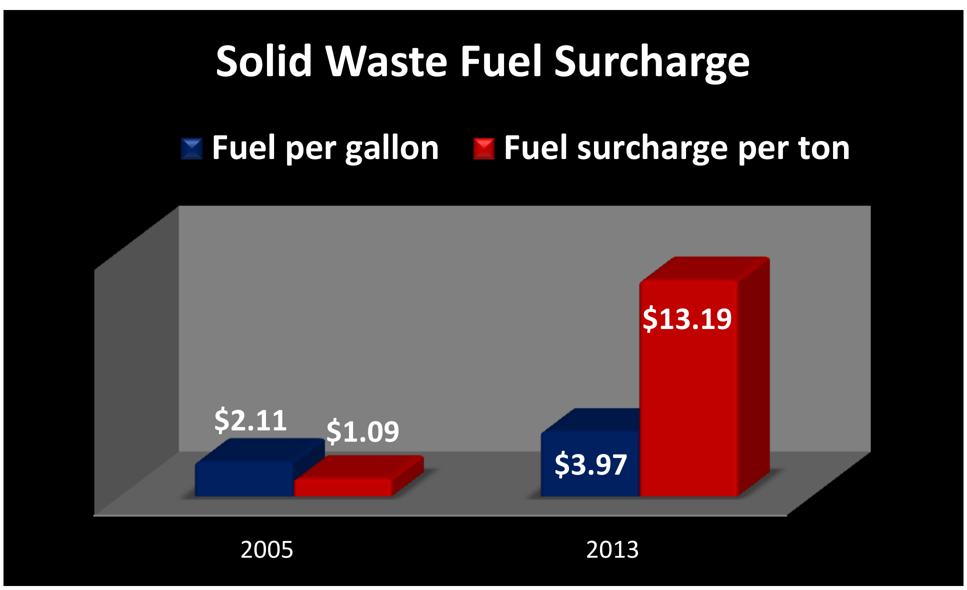
Solid Waste Enterprise Fund

One of the operations the general fund continues to subsidize is the solid waste enterprise fund. As of June 30, 2012, the solid waste enterprise fund had an accumulated deficit of $22.8 million. This deficit increased $2.5 million over the previous year, in spite of a $3.4 million transfer from the operating fund. Without this transfer the loss from operations was $5.9 million, which represents 28% of the revenues brought in. Rather than appropriately spreading the costs over all the entities benefiting from this service, property taxpayers are bearing a higher proportion of the cost of this fund.

Enterprise fund accounting is designed to highlight the extent to which fees and charges are sufficient to cover the cost of providing goods and services. Clearly the current revenue streams generated from the solid waste fund are not sufficient to cover the fund's current expenses.

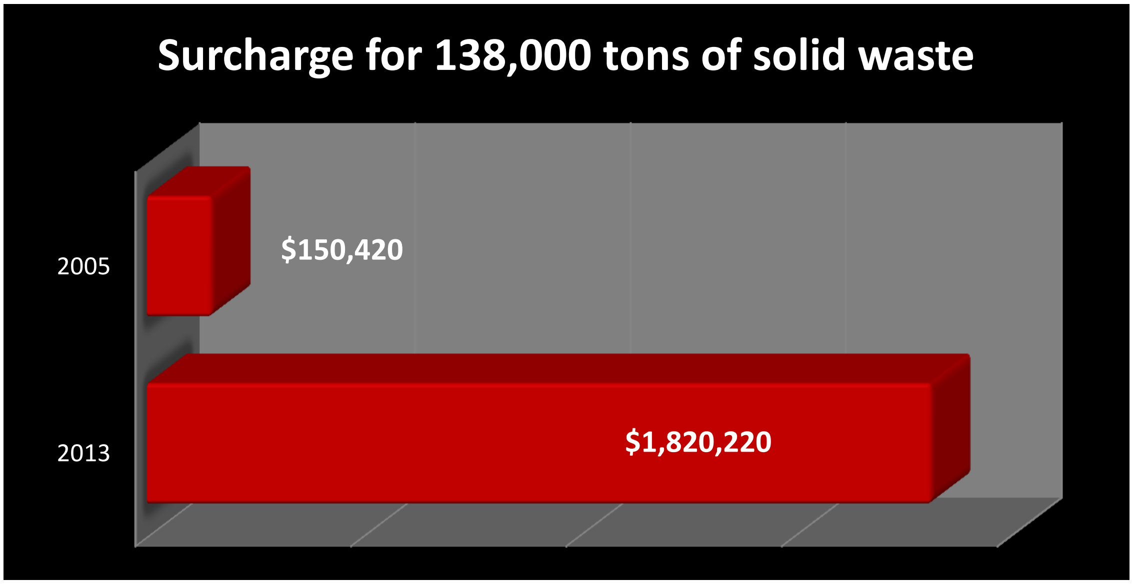
The contract for solid waste removal is expiring in two years. The current contract includes a fuel surcharge for moving waste to a landfill. This surcharge has increased significantly over recent years, which has resulted in increased expenses to the solid waste fund. The cost of transporting our solid waste has increased at a much greater rate than simply the percentage increase in gasoline prices.

To be specific, at inception of this contract July 1, 2005 the applicable price per gallon of diesel fuel was $2.11, which translated to a fuel surcharge of $1.09 per ton of solid waste. The current price per gallon of diesel fuel is $3.97, which translates to a fuel surcharge of $13.19.



This means that while gas prices have increased 88% over the past eight years, **the fuel surcharge has gone up more than 1300% during that same time period**.

Financially, this dramatic increase means that in 2005, the surcharge the City paid for transporting 138,000 tons of solid waste was $150,420, but now the City is paying more than $1.8 million for the same service.



The City should be mindful of potential other options for transportation costs to save expenses in the future contract.

Four-Year Plan

Included in the Comptroller's Budget Response last year was draft language for the Buffalo Fiscal Integrity Act, a plan to amend Article 20 of the City Charter to require a four-year financial plan. After being introduced by Council President Richard Fontana, the measure was unanimously passed by the Common Council on October 2, 2012, and signed into law by Mayor Byron Brown on October 22, 2012.

This is the first four-year plan submitted under the new law, which requires the Comptroller to opine on the sufficiency of the four-year plan.

Overall, the estimates of revenues and expenditures of the four-year plan do not appear to be unreasonable. However, there are some concerns that could become significant challenges down the road when considering that assumptions become more unreliable the farther out they are projected.

Many of the one-time revenues that the City has relied upon in the 2013-2014 budget – including fund balance, state aid held by the Buffalo Fiscal Stability Authority, parking funds, and Foreign Fire Insurance Tax receipts – will not be available to the same extent in the future.

While the City has not budgeted for its share of revenue from the Buffalo Creek Casino in past years, using $14 million in casino revenue, which the City has not received since 2010, in the four-year plan is risky considering the uncertainty surrounding the issue.

More than a third of the City's revenue comes in the form of aid from New York State, a source of income that we have little control over. In order to bring more security and stability to the City's finances, it is imperative other recurring sources of revenue are identified and pursued.