City of Buffalo

Department of Audit & Control

Budget Response

2014-2015 Fiscal Year
&
2014-2018 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 assessment of the Mayor's recommended budget for the Fiscal Year 2014-2015, as well as the 2014-2018 Four-Year Financial Plan.

As in the previous two years, the most alarming aspect of the 2014-2015 recommended budget is the structural budget deficit and the amount of fund balance used to close that gap. The 2014-2015 recommended budget anticipates the use of $27.5 million in reserves, an unprecedented amount that will weaken the City's strong cash position, which had been a major factor in improving Buffalo's bond ratings.

The other major concern is the unreliability of several significant sources of revenue, both in the 2014-2015 recommended budget and the four-year financial plan. Both the inclusion of some revenue sources that may not be available, as well as the amount of revenue that will be relied upon from other sources, appear to be overly optimistic. This overestimation of revenues could result in an even greater amount of reserves being needed to balance the budget, both in the next fiscal year, and subsequent years.

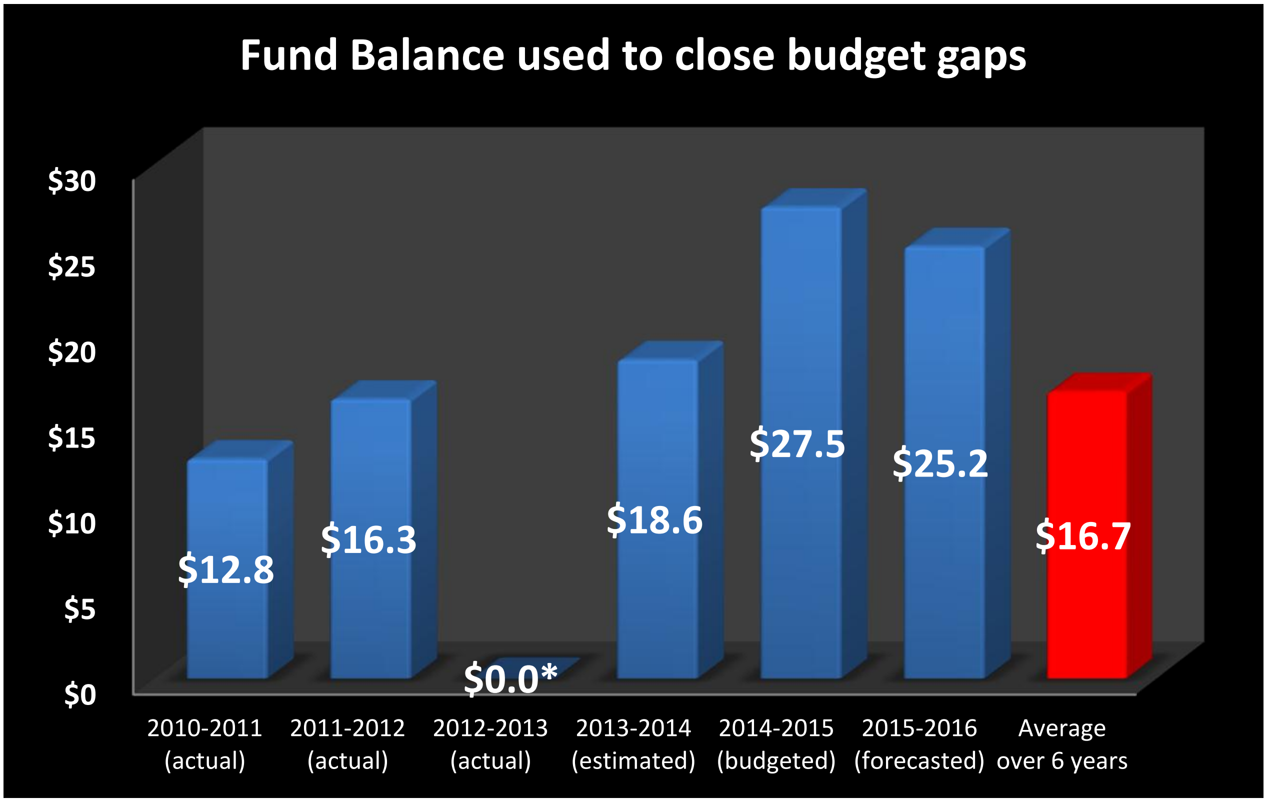
While the estimates of expenditures appear to be reasonable, the unpredictability of fuel and utility costs, as well as the upward trend of fringe benefit expenses, could pose significant challenges down the road.

The sweep of $7.5 million in revenue and all available reserves from the parking enterprise fund into the City's general fund, as well as the general fund's subsidization of the solid waste enterprise fund, continue to be of major concern. This on-going practice is a classic example of the old adage "robbing Peter to pay Paul."

The following pages, however, will focus on the overreliance on fund balance, as well as the uncertainty surrounding many sources of revenue.

Fund Balance

The $27.5 million in fund balance used to balance the 2014-2015 recommended budget is staggering, especially considering the amount used in recent years to address shortfalls. Despite not using any fund balance in the 2012-2013 fiscal year, the $27.5 million fund balance draw in fiscal year 2014-2015, and the $25.2 million fund balance draw forecasted in 2015-2016, would result in more than $100 million in reserves used over a six-year span, for an average of $16.7 million per year.



**Although a $15.6 million fund balance draw was budgeted for 2012-2013, unanticipated, non-recurring revenues in that year eliminated the need to use fund balance.*

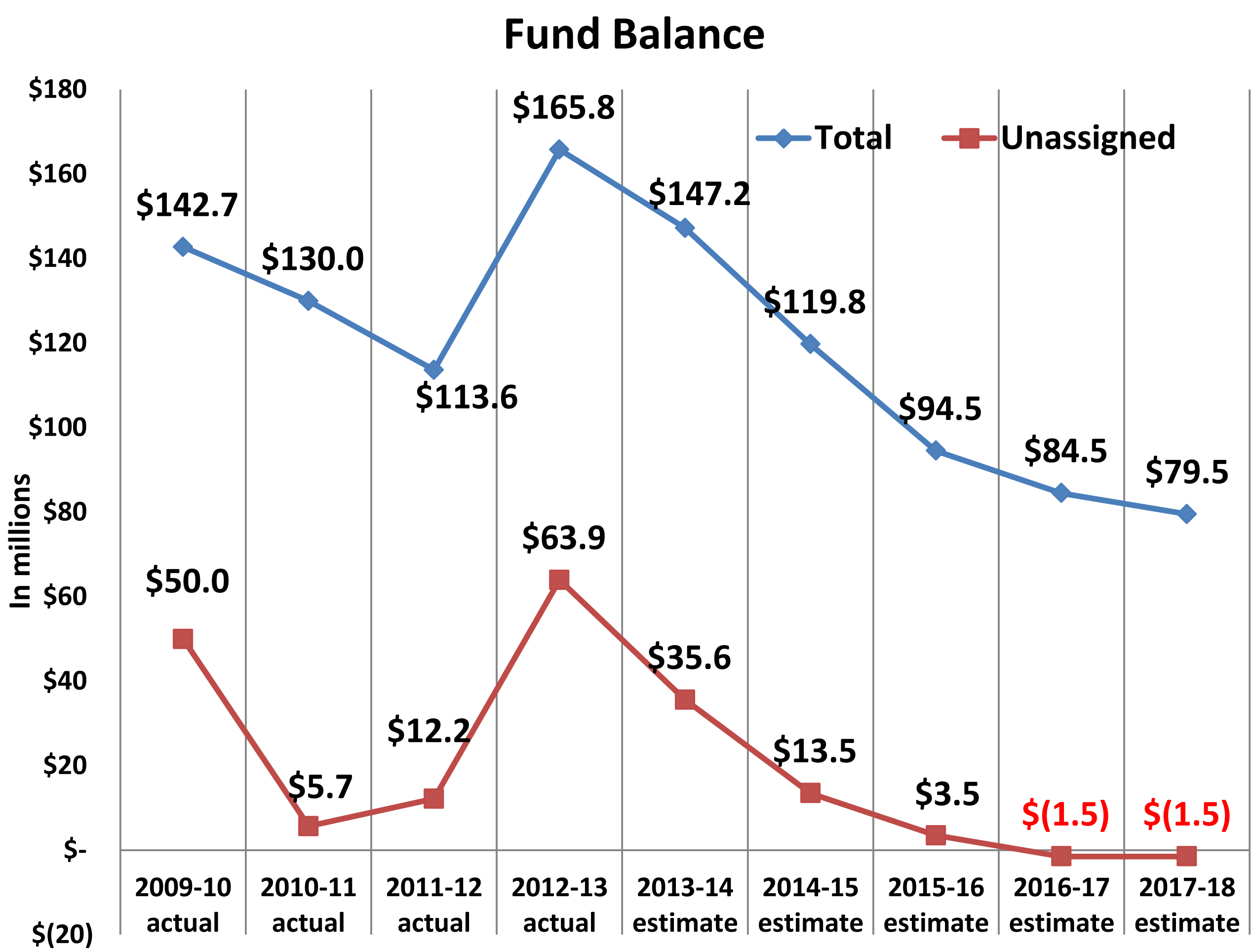
It is imperative that the City maintain a healthy fund balance. It is not a coincidence that the highest bond ratings in Buffalo's history were achieved at the same time that the City has a record total fund balance of $166 million.

When upgrading Buffalo from an "A" rating to an "A+" in March, Standard & Poor's cited the City's *"very strong reserve levels."* However, Standard & Poor's also indicated in its rating report that *"a significant deterioration in the city's reserve position, to levels less than those we consider very strong, could lead to our lowering the rating, given the city's limited revenue-raising flexibility and high fixed costs."*

When affirming Buffalo's "A1" rating in March, Moody's pointed to the City's *"solid reserve position and liquidity,"* while warning that *"continued use of reserves beyond what is currently expected"* and *"structurally imbalanced operating results"* could *"make the rating go down."*

Fitch's most recent rating report, affirming its "A+" rating of Buffalo, also cited the City's *"much improved reserve levels,"* but cautioned that *"the rating is sensitive to the city's ability to work towards consistently balanced operations and maintain reserves consistent with those projected in the current four-year plan."*

The City communicated to the rating agencies, prior to the issuing of these reports, that it plans to keep at least $100 million in total fund balance at all times. Unfortunately, the fund balance draws included in the recommended budget and four-year plan would result in a total fund balance below the $100 million benchmark by 2015-2016. Furthermore, the Unassigned category of fund balance – the only portion that can be used to balance the budget – would have a negative balance by 2016-2017.



Revenues

Several of the revenue sources in the recommended budget, and the amount to which they are relied upon, are considerably questionable.

For instance, $3.2 million in revenue is anticipated from traffic tickets, up $2.7 million from recent historical collections. This increase is attributed to the prospect of the City adjudicating its own tickets. While it is hopeful that New York State gives Buffalo the authority to do this, it is far from a sure thing. In order for the City to obtain such authority, Assembly Bill #A3702B and Senate Bill #S870B would both have to pass their respective houses in the New York State Legislature, and subsequently be signed into law by the Governor Andrew Cuomo.

Despite being introduced annually since 2007, this legislation has never passed both houses in the same year. Most recently, it failed to pass either house in 2013, and currently sits in the Senate finance committee and the Assembly transportation committee. While the Senate version did advance from the transportation committee to the finance committee on April 29, the bill has seen no movement in the Assembly since the 2014 version was introduced and referred to the transportation committee on January 8, 2014.

Even if the bill were to pass both houses and be signed into law by the governor this year, it would not take effect until January 1, 2015, halfway through the 2014-2015 fiscal year. So the $2.7 million in additional revenue would have to be achieved in a six month span. Not only is this uncertain revenue included in each year of the four-year plan, it experiences significant growth over the duration of the plan.

The budget also plans on the City receiving $5 million in revenue from the sale of city assets. The most revenue the City has ever attained in one year from selling its assets is $2 million. $2.8 million in revenue was budgeted for the sale of assets in the current fiscal year, and with less than two months remaining, the City has collected less than $500,000.

Revenue from the sale of City assets is included in each year of the four-year plan, with the $5 million budgeted in 2014-2015, $5 million forecasted in 2015-2016, $9 million in 2016-2017, and $8 million in 2017-2018, for a total of $27 million in four years. The Comptroller's office requested a list of properties that the City plans to sell in order to analyze the reliability of this revenue source, but it has not yet received this information.

Another uncertain source of revenue is $2 million resulting from the on-going analysis of the City's street light and electricity costs. Because the city must share any refund obtained from its electricity provider with Troy & Banks, the firm conducting the review, the City would need a $2.7 million refund in order to realize $2 million in revenue. A $2.7 million refund appears to be high, considering the previous $1.5 million settlement included only a $933,000 refund, with the remaining $600,000 of the settlement coming in the form of a decrease in future electricity bills spread over a four-year span. It appears that the $2 million is included as a recurring revenue source in the four-year plan, while any cash refund would likely be a one-time event.

The $2.2 million in revenue from building permits is more than double the previous year's amount, presumably from the anticipated increase in commercial building permit fees. We have not yet seen any evidence that this fee increase will lead to such a significant jump in revenue. To our knowledge, the ordinance amendment required to change the fee amounts has not yet been submitted to the Common Council.

$1.3 million in revenue is included via a transfer from the capital projects fund. While this transfer has been budgeted for in previous years, it has yet to come to fruition.

The budget also includes $3 million in revenue from state grants. At this time, we have no evidence that Buffalo has been awarded such grants.

The four-year plan also includes yearly increases in state aid in each year of the plan, ranging from 2 percent ($3.2 million) to 5 percent ($8.1 million). This is a risky assumption considering that state aid has remained flat in recent years. Relying on yearly increases in state aid, increases that are not in line with recent trends, only multiplies the potential risk of future budget shortfalls with each passing year.

The uncertain revenues discussed above total more than $15.2 million for the 2014-2015 fiscal year, and the inclusion of these revenues in four-year plan only increases the uncertainty surrounding the City's finances.

Conclusion

It appears the recommended budget and four-year plan were prepared envisioning a best-case-scenario unfolding. While many of the assumptions included in the budget are possible, the likelihood of all of them coming true is highly unlikely. It would be prudent to adopt more conservative budgeting practices that rely more on historical trends and solid evidence than speculative assumptions.

The lack of detail in the four-year plan makes thorough analysis of its validity extremely difficult. In the spirit of transparency, and in order to give a clearer picture of the City's financial future, a far more detailed four-year plan is essential.