

City Manager's 2022 Budget Message

October 11, 2021

TO: Mayor Bean, City Council Members, Key Staff, and General Public

FROM: Craig H. Cugini, City Manager

SUBJECT: 2022 Budget Message

Executive Summary

The City of Ishpeming 2022 budget reflects the many challenges that face the city. For many years, the City has experienced limited revenue growth and continued growth in expenses. The City's revenue has failed to keep up with continuously and significantly increasing fixed and unavoidable costs. This is compounded by further reductions in estimated revenues and increased costs related to the COVID-19 pandemic. While the City fared 2020 better than expected and 2021 has seen some return to normalcy, uncertainty remains as to the future funding levels from the State of Michigan as the State faces its own budgetary challenges. Tough choices have already been made to bring this budget proposal before you and to attempt to sustain the City's financial position. In 2020, the final approved budget for the General Fund showed a reduction of fund balance of \$(100,591); however, due to slightly higher revenues than estimated and a concerted effort by staff to reduce costs, the final 2020 result was to add \$13,210 to fund balance. For 2021, The General Fund budget showed a reduction in fund balance of \$(203,119); however, management is currently estimating ending 2021 with a reduction of fund balance of \$(233,455), which is \$30,336 more than originally planned. For the 2022 budget year, the City continues to take a conservative position in regards to budgeting by presenting a "worst-case scenario" approach this is favored by Standard and Poor's, the City's bond credit rating agency. As such, the 2022 General Fund budget show a reduction in fund balance of \$(187,085). As management has successfully achieved in the past, staff will continue to work on cost saving measures to try to improve performance over current "worst-case scenario" expectations.

The City must get on a sustainable path. The MERS unfunded liability is the largest of the financial problems facing the City, but by no means the only one. The City of Ishpeming negotiated with the unions to close the MERS defined benefit pension plan to new hires after January 1, 2020; however, the existing liability continues to grow exponentially. The funded level of the MERS defined benefit pension plan was 48% funded as of 12/31/2020. In response to this measure, on September 13, 2021, the City was granted the authority by the Michigan Department of Treasury to issue pension bonds in order to fund up to 95% of the actuarial liabilities. Issuing these pension bonds is projected to stabilize the annual contribution moving forward and potentially save the City an estimated \$5.3 million over the life of the bonds.

Outline of Budget Message

There are three sections to this budget message:

1. Expected Outcome of 2021-summary of the expected financial position ending 2021
2. Proposals for 2022-highlights of proposed financial plans for on-going services
3. Financial Problems and Opportunities-looking at some options for the future

Note: This budget message does not review every fund. To keep the message brief, I cover only major funds or funds with specific problems.

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Section 1 - Expected Outcome of 2021

2021 – 101 General Fund

Staff projects the Fund Balance for the General Fund to be \$677,497 at the end of 2021, a decrease of \$233,455 from beginning fund balance of \$910,952.

2021 – 202 Major Street Fund and 203 Local Street Fund

Fund Balance for Major Streets is expected to increase by \$176,056 to \$934,202 at the end of 2021. We are building up the fund to pay for future street construction work. Fund balance for Local Streets is expected to increase by \$5,154 to \$137,071 at the end of 2021. The 2020-21 winter saw a reduction in snowfall than the previous two winter seasons that has led to decreased winter maintenance costs resulting in excess funding provided by the Michigan Department of Transportation.

2021 - 206 Special Fire Fund (Fire Truck Purchase)

Fund Balance for the Special Fire Fund is expected to increase \$26,884, ending 2021 at \$94,174. This fund is used to record the tax revenue for the voted millage used to purchase a fire truck as well as recording the payments on the fire truck.

2021 – 211 Fire Fighter Longevity Fund

Fund Balance is expected to end the year at \$211,677. Any payments out will be made per policy covering Fire fighter retirees.

2021 – 226 Garbage Fund

The Garbage Fund fund balance is expected to end 2021 at \$265,527, an increase of \$16,400. The planned spend-down of this fund was begun in 2014. In 2018 Council began to raise rates to end the decline. While garbage rates will need to increase over time to generate revenues necessary to meet the continuing tipping fee increases at the Marquette County Solid Waste Management Authority, at this time staff is not proposing a garbage rate fee increase for 2022.

2021 – 248 Downtown Development Authority (DDA)

For 2021, the DDA fund balance is expected to end at \$666,320, down by \$49,759, which is better than the original planned spend down of \$63,678. Of this, \$484,213 of the DDA's fund balance is restricted.

2021 - 401 Public Improvement Fund

In 2021, the Fund Balance for the Public Improvement Fund is projected to increase \$93,008 to \$442,926. We need to build this fund to pay for much needed projects throughout the city.

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2020 – 590 Sewer Funds

Sewer Fund is projected to end 2021 with an unrestricted net position of \$964,995, which is up \$399,339. The City has been working towards the goal of beginning a sewer infrastructure replacement project in the future.

2021 – 591 Water Fund

The Water Fund is expected to end 2021 with an unrestricted net position of \$272,741, which is an increase of \$612,467 over the prior year's deficit. The City of Ishpeming was also awarded a Financially Distressed Communities Grant from the State of Michigan in the amount of \$250,000 to be used to purchase water meters and radio read units, which is currently being executed.

2021 – 661 Motor Pool Fund

This fund was established in 2018 with an initial fund balance of \$30,000. It is expected to end 2021 with an unrestricted net position of \$117,936, down \$222,116 due to investment in new equipment during 2021. The goal is to continue to work on growing this fund with ultimate goal of replacing vehicles and equipment without borrowing money to do so.

The City's other funds remain healthy and are operating as planned. Please refer to the details budget sheets in the budget proposal document.

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Section 2 - 2022 Proposal

Taxable Values and Millage Rate

Based on information from the County Equalization Department, the City's 2021 taxable value (the 2021 value is used to compute the 2022 tax collection) is \$126,597,250. The City Council has adopted a tax levy (Millage) with revenues:

Tax category	Millage	Tax Revenues*
Operations:	13.1795	\$1,552,390
Act 345 Retirement:	2.8197	\$291,919
Public Improvement:	4.3930	\$517,436
Fire Equipment	0.8822	\$111,918
Total:	21.2744	\$2,578,302

*Note: Tax Revenues are subject to change based on Board of Review, Tax Tribunal, or other adjustments. It is certain there will be some reductions; however, they are not expected to be major. City revenues are reduced by the DDA recapture which is estimated to be \$253,515.

2022 - 101 General Fund

Staff projects General Fund revenues of \$2,896,443 and expenses of \$3,083,528, using \$187,085 from Fund Balance to provide a balanced budget. As previously discussed, this is a "worst-case scenario," and, as in prior years, staff will continue to work at reducing expenditures in order to improve the financial outlook.

The COVID-19 pandemic has led to reductions in revenues from sources such as rental and tube slide income; however, it is yet uncertain as to how a prolonged pandemic will impact revenues or how stable the funding from the State of Michigan will be. At this time, the outcome of the health insurance renewal for 2022 is still unknown. The proposed budget includes annual contribution to UPSET of \$10,000 and a payment of \$9,000 to the Senior Center.

To preserve the City's financial position, I recommend we set future budget meetings to discuss area we can reduce costs and develop plans for long-term sustainability of the City's operations. If the proposed budget is executed as planned, the fund balance will be about \$490,412 at the end of 2022. This fund balance level is about 15.9 percent of the 2022 expected expenses—a decline of about 5.5 percent from 2021.

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2022 – 202 Major Street Fund and 203 Local Street Fund

Condition of some City streets has significantly improved due to the USDA project. Unfortunately, we still have a lot of streets needing help. Due to action of the State in prior years, our Major Street funding is up somewhat; however, the City's winter maintenance costs have decreased last winter due to decreased snowfall. The 2022 budget anticipates an average year of snowfall, but our intent is to try to reduce overtime costs and reduce the overall winter maintenance costs. In the past, increased winter maintenance costs have been a drag on the Local Street budget.

State of Michigan action to increase funding a couple years ago, while a positive step, did not fully correct the state-wide shortage in road funding. Even with the increased Act 51 revenue, the City is unable to keep up with basic maintenance expenses, purchase equipment and supplies, and apply the appropriate repairs to maintain deteriorating streets. The 2021 budget proposed transferring \$300,000 from the Public Improvement Fund to the Local Street Fund in order to put \$400,000 towards street paving. This \$300,000 transfer did not take place in 2021, but it is included in the 2022 budget in order to leverage grant funding for planned road infrastructure projects.

In 2022, this budget shows Major Street revenues of \$1,227,180 and expenses of \$1,421,212, which includes a \$100,000 transfer to the Local Street Fund preservation of the local street system as allowed under Act 51. This will draw \$194,032 from the fund balance, resulting in a Major Street Fund Balance of \$740,170 at the end of 2022.

In 2022, the Local Street Fund, we plan to spend \$869,786, which includes \$400,000 of street paving, with revenue of \$927,270, which includes \$100,000 from the Major Street Fund and \$305,000 from the Public Improvement Fund. The difference of \$57,484 will be added to fund balance, resulting in an expected Local Street Fund Balance of \$194,555 at the end of 2022.

2022 – 226 Garbage Fund

In 2022, the fund is expected to spend \$782,130 against revenues of \$796,480. The projected 2022 ending Fund Balance of the Garbage Fund is \$279,877, up \$14,350. Council approved an increase in the Residential Waste Disposal Fee in 2021 of \$1.00 per month for a monthly fee of \$21.90; however, there is no recommended increase to the Residential Waste Disposal Fee in 2022. The Marquette County Solid Waste Management Authority tipping fee has gone from \$49.50 per ton in 2019 to \$61.50 per ton for its fiscal year 2021-2022. Marquette County Solid Waste Management Authority is projecting an annual \$2.00 increase in the per ton tipping fee until it reaches \$69.50 in its 2025-2026 fiscal year. This planned fee schedule by Marquette County Solid Waste Management Authority will require annual increases to the City of Ishpeming garbage customers. The Council may wish to discuss this rate increase during the budget workshop.

2022 - 248 Downtown Development Authority (DDA)

In 2022, the Downtown Development Authority (DDA) Fund has increased spending capacity due to refunding of its 2011 Capital Improvement Bond, which issued a new bond at a lower interest rate which is estimated to save the DDA \$170,470 over the life of the bond. because of high bond payment

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levels, although the DDA bond payments peaked in 2020 and will now decline over the next couple years. Therefore, in 2022 the DDA will not need to utilize fund balance to make investments into the downtown. This means that expenses will be lower than the revenues in 2022. With about \$253,715 in revenue in 2022 and \$237,060 in expenses, the DDA will add \$16,555 to the fund balance to fund a skate park, assist in a forest management plan, renew the façade grant program, and invest in new holiday lighting.

2022 - 401 Public Improvement Fund

The fund expects revenues of \$522,236 and expenses of about \$538,998, resulting in a decrease of \$16,762 in the fund balance. The Public Improvement Fund has committed debt payments of \$220,598, which leaves \$318,400 available for use in 2022. As previously mentioned, the available \$305,000 will be transferred to the Local Street Fund to go towards street paving. All other spending that normally would come from the Public Improvement Fund will be placed on hold until the 2023 fiscal year.

2022 - 590 Sewer Fund

The Sewer Fund is expected to have \$1,689,300 in revenues against \$1,555,523 in expenses, giving a boost of \$133,777 to fund balance by the end of 2022. Recently, Council approved the feasibility of obtaining grant funding and/or low interest loans in order to move forward with a much-needed sewer infrastructure project. Currently, the ordinance for the Sewer Fund requires an annual 5 percent increase in the sewer rate.

2022 - 591 Water Fund

The Water Fund remained in deficit in 2020, but the deficit was reduced to such a level that the City of Ishpeming was no longer required to report the deficit to the Michigan Department of Treasury. The deficit was created several years ago by extreme cold weather conditions and by previously unreimbursed expenses related to the USDA project. The plan is to continue working to fully eliminate the deficit in the Water Fund. It is anticipated that the deficit will be fully eliminated by the end of 2021. In 2022, revenues are expected to be \$2,610,590 with expenses of \$2,161,899 resulting in net income of \$448,691 and an ending unrestricted net position \$721,432.

2022 - 661 Motor Pool Fund

This was a new fund for the City of Ishpeming in 2018. It consolidates the revenues and expenses related to DPW equipment operations and maintenance from several other funds, including: General Fund, Public Improvement Fund, Water Fund, Sewer Fund, and Street Funds. The idea of this fund is to provide direct public visibility of the funds used with this important fleet. This fund has grown since its inception, and the City has been able to purchase a couple significant pieces of equipment from this fund. In 2022, total revenues for this fund are expected to be \$586,000 with expenses of \$692,350, including depreciation, resulting in an ending unrestricted net position of \$11,586. These 2022 expenses also include \$50,000 for capitalizable equipment purchases.

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Section 3 Financial Issues and Opportunities

As described above, the City continues to look at opportunities to obtain grant funding, look for ways to grow revenue, and seek solutions to some of the financial challenges. Topics of discussion here are about some of these important financial consideration for the future. The areas below are items that could be considered in future budget meetings as we seek a sustainable path for the City of Ishpeming.

New Revenue Sources

To keep up with cost growth, the City needs new revenue. Unfortunately, **none** of these may be put in place for the 2022 fiscal year. All would require action in 2022 to implement in 2023.

A. Library Millage

Under Act 164, the City Council is authorized to levy 1 mill to pay for public library expenses. The City currently does not levy this tax, but pays for the entire cost of the Library out of other sources of revenue, including the General Fund. The soonest that the City could use this millage as a source of funding in the 2023 budget. The idea of this millage is that by dedicating this new specific tax to the Library, the City will free up tax revenue for other needs. This increase in taxation would bring in about \$120,000, costing the average tax payer about \$50 per year.

B. Headlee Override

With the correct legal process (see attached Fact Sheet and sample ballot language), the City has a legal means to override the Headlee Amendment, returning the millage rate for the City of Ishpeming to the maximum constitutional rate of 20.9 mills. Currently, the City levies 18.4547 mills between General Operating and Public Improvement Fund. Therefore, using this process could gain the City about 2.4 mills (or about \$280,000) of new revenue. This action requires a public vote, which could be defeated.

C. Voted Millages

Similar to the Fire Truck Ballot Proposal, the City has the authority to place a wide variety of specific ballot initiatives before the voters. This choice could help with various expenses, including providing funding for road improvements or park maintenance.

Reducing Costs Via Employee Healthcare

While the City of Ishpeming reviews its healthcare costs on an annual basis in order to obtain the best outcome, healthcare costs continue to be a significant portion of the budget. The City Healthcare Committee should convene in order to explore options to further reduce this cost while maintaining reasonable healthcare for employees.

Reducing Costs Via Employee Healthcare (continued)

Under Public Act 152, the City Council must vote in 2021 by a super majority (4-1) to continue this total support into 2022. Per State law, if this policy is not continued the City must move to either an 80/20 cost share or to pay not more than a fixed "cap" per employee. The State of Michigan sets the cap annually. Either of these options would force the employees to pay a substantially larger share of healthcare costs in the form of payroll deductions. Some form of healthcare premium cost-sharing with our employees is going to be necessary in the future.

Craig H. Cugini
City Manager