

# City of Flagstaff

June 30, 2008

#### Dear Mayor and City Council:

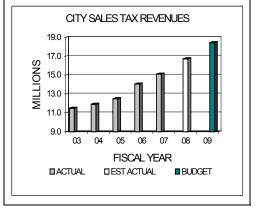
It is with great consideration that I submit to you my first Manager's Recommended Budget. How we spend the public's money is our most important business. This proposal is for FY 2008-2009 with an eye towards our financial future for the next five years. I arrive at a time of significant financial uncertainty across the state of Arizona and the nation. For Flagstaff, our financial picture is a bit brighter than our peer cities due

to our economic development efforts of the past few years, but is also susceptible to any financial stagnation in the retail, tourism and/or construction segments that fund our municipal corporation.

The economic development work associated with Aspen Place at Sawmill, the Incubator, the expansion of the Flagstaff Mall, the auto-mall, and the contributions to the High Country Conference Center and now the State's capital infusion into Northern Arizona University, position Flagstaff to grow new revenue generators while other generators may stabilize or falter. These efforts shift construction associated revenues from the stalled residential market to the commercial market and offer greater retail opportunities for consumers and replacement revenue for governments. Our current estimate is a growth in sales tax revenue of approximately 10%. The following graph illustrates our historical and anticipated city sales tax growth:

The introduction of new non-stop air service to Southern California is another economic development effort that will assist in out-of-state bookings to Flagstaff and the new conference center which will in turn lead to greater tourism related expenditures also known as Bed, Board & Booze

CITY SALES TAX			
FY:	AMOUNT	% CHANGE	
02-03	11,500,467	3.3%	
03-04	11,917,786	3.6%	
04-05	12,500,038	4.9%	
05-06	14,054,056	12.4%	
06-07	15,109,645	7.5%	
07-08	16,720,191	10.7%	
08-09	18,440,121	10.3%	



(BBB) revenue. This air service also serves as an important business retention program as some of our largest employers, W.L. Gore and Northern Arizona University among them, have greater access to their customers and partners and feel less pull towards the Valley for establishing business operations.

All of this being said, the greatest uncertainty when developing the proposed budget was the fiscal health of the State. Now that a state budget has been adopted, we have a better idea of its impact upon Flagstaff. The City of Flagstaff budgeted an amount of state shared **sales tax** that is equivalent to what the state has budgeted. The state has budgeted \$137,000 more in state shared **income tax** than we originally budgeted. However, the amount of Highway User Revenue Funds (HURF) to be shared will decrease \$500,000 - \$600,000. Staff will need to confer with Council on how this shortfall will be addressed. It is our intent to absorb as much as possible within this earmarked fund and not look to the General Fund for changes. We had already projected state revenue sharing conservatively to the point that it offset much of the anticipated growth in sales tax at the local level setting our overall revenue growth for the General Fund at only 3% (excluding the Aquaplex and sales tax triggers).

Given these financial conditions, the Council Adopted Budget focuses upon meeting existing and previously made commitments first and foremost while addressing pressures to preserve existing service levels increases. Furthermore, departments were asked to compare their requests for new dollars against the lowest 1% priority from within their base budget in order to determine if there are trade-offs in expenditures that better address current program delivery. Lastly, departments and the Budget Team identified how existing programs, as well as new requests, help advance the five Council priorities of Economic Development, Affordable Housing, Facilities, Water Resources, and Competitive Employee Compensation. I will highlight these efforts later in the message under Council Goals.

#### **Existing Commitments**

In the General Fund, our revenue forecasts translate into approximately \$2.2 million in new revenue. Unfortunately, state and federal mandates as well as existing commitments to programs reduce this amount fairly quickly.

New ongoing revenue Other budget changes Total available	\$2,200,000 <u>300,000</u> \$2,500,000	
Police PSPRS	(\$	400,000)
Fire PSPRS	(\$	250,000)
Keeping Employees Whole	(\$	645,000)
Energy Increases	(\$	100,000)
Aquaplex	(\$	600,000)
Gas & Oil Increases	(\$	50,000)
Airport Security	(\$	200,000)
Cost Allocation Reduction	<u>(\$</u>	250,000)
Available Ongoing	\$	5.000

The Public Safety Personnel Retirement System (PSPRS) plan is experiencing severe financial difficulties for numerous reasons including poor returns and increased benefits during peak returns. Consequently, employer contributions to PSPRS will increase significantly. This, combined with merit increases and other benefit cost increases, will keep employees whole (meaning their take-home pay does not decrease in FY '09). Keeping employees whole is critical as we continue to face rising turnover due to uncompetitive wages and the high cost of living in Flagstaff.

Additionally, inflation associated with energy and oil continues to impact our budget. While numerous conservation efforts are in place and expanding, our overall energy consumption will grow in 2008-2009 primarily attributable to the Aquaplex opening in August 2008. This is a sizeable new facility. While its energy demands have been mitigated through green technology, these are not sufficient to have a net neutral effect on our bottom line.

Airport security is an issue in which we have minimal control. As the nation continues to function under a Homeland Security level orange, we are required to provide someone with arresting powers at the airport during times of Transportation Security Administration (TSA) screening. This has been accomplished, with temporary approval by the Federal Aviation Administration (FAA), through overtime assignments by the police department or by pulling existing personnel off their beat to monitor the screening. With additional flights and pressure by the FAA to fully comply, we must add four new police officers to meet the requirements. This could certainly be accomplished by a reassignment of existing police personnel, but this would reduce the strengthened efforts that have been made in recent years to combat above average property crime and focus resource on community policing in the Sunnyside Neighborhood.

The last item, Cost Allocation Reduction, is an internal administrative measure that results in a real dollar decrease to the General Fund. As you know, much of our administrative overhead is appropriated in the General Fund. This includes the City Manager's Office, Finance, Human Resources, Information Technology etc. These administrative costs are charged to other funds based upon a formula. A recent reassessment of these charges found that the General Fund was overcharging other funds by approximately \$250,000. The good news is that this provides additional revenue for those other funds. The bad news is that the General Fund, with the greatest array of programs and services, has fewer discretionary dollars to meet new demands.

Another existing commitment, whose funding will come from the General Fund, but is tied to an earmarked revenue source, is the Downtown Management Plan. The Downtown manager and ambassadors are funded from meter revenue. I consider this an existing commitment, but not one that is impacting our ongoing funds.

Due to these commitments, the amount of ongoing funds available in the General Fund is extremely limited. Personnel considerations should be funded with ongoing dollars in order to avoid the organizational and program instability that comes with constant hiring and terminations based upon the availability of one time money. Consequently, we focused personnel expenditures on requests that were addressing the growth of existing services or programs (such as dispatch call taker or park maintenance) and internal reorganizations that looked to increase efficiency and effectiveness. In total, there was sufficient ongoing dollars to add 3.75 FTE in the General Fund not including the police officers. There is also three new paramedic and four new phlebotomist assignment pay slots funded.

Another General Fund personnel expenditure that I would like to call attention to is the addition of fire fighters in conjunctions with the SAFER grant. Due to the extreme limitation in ongoing dollars we were not in a position to accept what might have been a grant award of six full time fire fighters. This is a five-year grant in which the federal government pays approximately 35% of our fire fighter's salary. I believe we can sustain three new fire fighters. Unfortunately, due to the inflexibility of the grant, we were not able to reduce our request to three. However, we have submitted a new application for the current SAFER grant cycle in which awards are anticipated prior to November. On this basis, \$60,000 in ongoing funds has been earmarked in this budget to provide Flagstaff's match to a SAFER three-person award. If the grant is not received, we will look to use the \$60,000 to hire three non-grant funded firefighters in the fourth quarter of this budget. Moreover, \$200,000 in one-time money in the Fleet Fund has been recommended for a Rescue Unit that would be available in February 2009 and \$125,000 in one time money from the Real-Estate fund has been allocated to the Fire Training Center.

To address the remaining non-personnel requests for revised services level (RSLs) increases, we had to turn to one-time revenue. In some cases these were capital expenditures such as vehicles or facility related, but in most cases these were ongoing expenditures in which the department must re-request the full amount next year or face a cut in the service. In total, there is \$580,000 in ongoing RSL's that are funded with one-time dollars. While some may find this use of one-time dollars lacks the more conservative nature needed to address our situation, I found the expenditures necessary to address the growing demand for existing programs and services. We continue to see added acreage in parks, medians, rights-of-way, and the Flagstaff Urban Trails System (FUTS) from already committed capital projects. Computer software maintenance agreements have inflated either by increased licenses or other terms but are essential to keeping our programs up and running.

Related to the topic of computers, our use of technology and technology infrastructure is lagging and needs a boost. One-time dollars have been appropriated to assist in improving various aspects such as transactional e-government (for example permits, parks & recreation registration, forms submittals, etc.), push technology (most commonly known in Blackberry's), and office automation (copiers/scanners & document imaging). These will increase employee efficiency and make city services more accessible & convenient.

#### **Council Goals**

In February, the City Council conducted a mini-retreat in which it identified numerous worthy programs and services meriting consideration as top city priorities. After some voting, five priorities emerged. These were Economic Development, Affordable Housing, Facilities, Water Resources, and Competitive Employee Compensation. The Council further refined these goals to provide staff some focus and identify the overall desired outcome of the efforts. This work is articulated as follows:

Economic Development – How can we facilitate an increase in the Annual Median Income (AMI)?

How can we maximize investments (Conference Center, Sawmill, Mall, Airport, the Incubator)?

What can we do to enhance the opportunities for business development?

How do we build on our strengths to create anchor industries and bring budding ideas to the market?

How do we encourage public/private partnerships?

How do we align the labor supply with labor demand?

Affordable Housing – How can we facilitate an increased supply of homes between \$150,000 - \$280,000 (80-150% of Annual Median Income (AMI))?

Facilities – How do we remedy inefficient, out-grown facilities that are not in the public eye?

How do we develop appropriate facilities in a strategic manner that recognizes competition for bond money, priorities of the organization and is supportive by the community?

Water Resources – How do we secure our water future for the next 100 years?

How do we increase demand and supply for reclaimed water?

Compensation – How do we retain and attract employees in order to serve the needs of our community?

How do we ensure internal and external equity amongst employees?

How do we incentivize performance?

How can we mitigate the impact of housing costs?

Many of these efforts are underway and don't require significant, if any, new funding. Council and this community have made substantial investments in economic development, affordable housing and water resources in recent years. As a result, we have personnel developing and implementing programs to answer many of the questions posed above. Not just in paper but in actions. Some examples of progress towards these goals that is anticipated in Fiscal Year 2008-2009 include:

# **Economic Development**

- ❖ The opening of the Northern Arizona Science, Technology and Clean Energy Center (the incubator) with an anticipated occupancy of greater that 80%
- New air service between Flagstaff and Los Angeles;
- ❖ Work Force Development including funding of the "WorkKeys" program in partnership with CCC, the County, NAU and private companies;
- ❖ The implementation of the University to Business Connection Program in partnership with Northern Arizona University;
- Ongoing support to implement the Northern Arizona Bioscience Roadmap including financial support of Science Foundation Arizona in partnership with the Flagstaff 40;
- ❖ Visitations to at least three businesses per month to understand their business retention and expansion needs, and using existing programs or developing new ones to meet those needs;
- Major expansion of Nestle Purina PetCare facility;
- Upgrading of the CityofInnovation.com Web site to create a single source portal for local businesses seeking assistance and for companies looking to relocate;
- Creation of an online database system to track trade show attendance, leads generated and necessary follow up related to business attraction and business retention and expansion;
- New Partnership with the Arizona Department of Commerce to promote the Flagstaff Innovation Park and the available land at the airpark to site selectors and potential relocating companies:
- Plans for a new retail development at Fourth Street and Route 66, a new public/private partnership.

#### Affordable Housing

- Development of 16 units on Izabel North in FY 08-09;
- Development of 22-26 units in Schultz Pass possible in FY 08-09;
- Continue work on Development Agreement for development the J.W. Powell property, resulting in a minimum of 125 units;
- Completion of the Rio Homes project, bringing the unit total to 30;
- Development of partnerships for employer assisted housing programs;
- Continued partnerships with the private development community for workforce housing units;
- Work to address homelessness with a broad community discussion and program implementation plan;
- Completion of set-aside policy rewrite.

#### Water Resources

- Award contract for feasibility study of Red Gap Ranch Pipeline:
- Complete analysis of Flagstaff Water Adequacy program;
- Bring four new wells on-line;
- Negotiate groundwater allocation at Red Gap:
- Continue involvement in the Western Navajo Pipeline discussions;
- Participation in regional water partnership groups.

#### Facilities

- Complete Municipal Court Space Study;
- Complete City Space Needs Study & Facilities Master Plan;
- Identify site for Public Works Maintenance Facility;
- Construct Cemetery office building in order to meet with families indoors;
- Construct Fire Station 3:
- Award Contract for Fire Station 2:
- Determine & Fund Fire Administration location;
- Purchase & locate Fire Training facility;
- Complete Parking garage Feasibility Study.

#### Compensation

- Articulate management and Council commitment to competitive compensation;
- Conduct a compensation study to remove assortment of disjointed fixes;
- Move employee wages closer to middle of the market;
- Identify measures to stop immediate losses of police and dispatch personnel.

Below I will provide more details regarding the compensation proposals encompassed in this budget, but I first want to call your attention to an important related point regarding accomplishing the Council's priorities. It would be very easy as the City Manager to point to the various departments or divisions who are dedicated to these particular goals (ex. Community Investment for Economic Development and Affordable Housing), but we must orient the entire organizations towards making progress on these five goals. As you read the material in the budget, you will find individual department, division and section efforts towards these goals under the caption FY-09 New Initiatives. As we make this format a part of our annual budget process, I believe the coordination and ideas will strengthen and become more prominent and tangible.

#### Compensation

The City of Flagstaff as a municipal corporation is a service organization. In other words, we primarily provide services. Retaining and attracting personnel is key to providing the services this community demands. The disparity between housing costs and income have been a significant factor in increasing our turnover and impeding our recruitment efforts in many positions. Moreover, our most recent compensation survey indicated that our wages are anywhere from 6-12% below the market average. Therefore, more attention must be focused on taking care of the people we have before adding new positions. However, as noted above, we have very limited on-going funds available for FY 09. Therefore, I am proposing the following compensation efforts:

# 1) Keeping Employees Whole

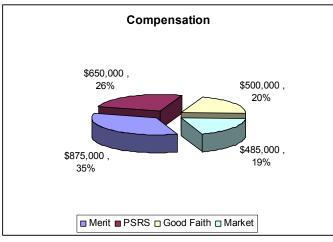
Under the section entitled existing commitments, I called out the significant monetary contributions that the city must make to the Public Safety Personnel Retirement System. This \$650,000 enables the existing benefits to remain untouched. The second item entitled "keeping employees whole" budgets a 3.2% merit or step increase for all eligible employees, plus any increase in benefit costs which is another \$645,000 commitment from the General Fund, \$875,000 citywide.

### 2) 1% Market Increase

In our initial budget projections, we anticipated a health and dental insurance rate increase of ten percent. The actual increase came in at 1.8% for health and a decrease of over 9% on dental. The difference between that projected amount and the actual cost was enough to award a 1% market increase city wide. This is a \$375,000 ongoing expenditure to the General Fund, \$485,000 citywide.



Items one and two above will not be sufficient to stave off turnover, particularly for patrol officers and dispatchers that are in high demand state and nation-wide and in which the competition has become particularly fierce. We are aware



of double digit increases in police salaries in the Valley and signing bonuses greater than \$10,000 in that same market. Therefore, we are proposing taking \$500,000 in one time dollars and paying for one year a 5% retention pay to all patrol officers, dispatchers and 2% to corporals (estimated cost \$250,000) and then providing a one-time good

faith bonus to all other employees mid-fiscal year (December 2008). The good faith bonus would be staggered depending upon tenure with a maximum of \$400. Neither of these tools may be sufficient to completely stop the migration to better paying jobs in other communities, but they help and they show an acknowledgement of the situation and a commitment to explore long term compensation strategies.

## 4) Market Triggers

This is a new concept for the City of Flagstaff. Much of our revenue forecasts are conservative not only due to the economic uncertainty statewide, but many of the new revenue producers (the Sawmill, the Mall expansion, the Auto Mall, and the Conference Center) are not yet developed. We are also bringing in new stores in which we do not have a proven revenue history to rely upon. Consequently, we have projected conservatively. The market triggers say that if revenue come in higher than projected, we will dedicate those first ongoing dollars to compensation increases (i.e. getting the base salary closer to the middle of the market). In short, we have established a revenue benchmark for state and local sales tax revenue reflecting June 2008 through December 2008 sales. For every 2% we exceed that benchmark, a 1% market increase will be awarded on the first pay period in April 2009, for a maximum of a 2% market increase. This is not retro-active. Both the benchmark and the actual receipt will be verified by our external auditors to ensure impartiality.

While this concept it new, it is not unproven. We used this concept in the city of Boulder to get through a recession and the rebuild of the regional mall. The program was very successful and bought credibility with employees and eventually market competitiveness. I believe both will come true here. It further demonstrates a clear commitment to our employees that compensation is a high priority.

Combined, I believe these four efforts, along with the compensation study, will put us on a stronger path towards reduced turnover and competitive attraction efforts. They may also raise the AMI which will lead to more housing opportunities for our employees.

#### **Other Funds**

Obviously, the financial picture of the City includes many other funds that are impacted by compensation decisions and current economic conditions. Most of our special revenue funds are closely tied to the economy. This would include the BBB and transportation funds. These funds support ongoing operations associated with tourism, economic development, transit, and provide the financial engine to build essential infrastructure in the community such as roads and trails that contribute to the City's quality of place. BBB revenue in 2008-2009 is expected to rise minimally. The City's HURF funds are dependent on the fuel sales statewide and have been decreased for FY 09. This compounds the challenge to adequately meet the ongoing and growing demands of maintaining our roadways including the overlay program. With flat revenues and significant inflation of road construction materials, these programs will make smaller and smaller increments of progress.

All three of the enterprise funds received modest rate increase in 2008 and some are planned for 2009. The Water and Sewer fund has depleted most of the cash reserves to pay for the Wildcat Hill Plant upgrade and has had to make adjustments in their capital plan. As noted above, the City is also investing heavily in meeting long-term water demand. The timing of these investments is appropriate as state laws have changed and negotiations with state, federal and Indian parties continue. From an operating stand-point, energy costs to pump and treat water continue to erode our efficiency. While pumping water from Upper Lake Mary is cheaper than pumping from wells, the increase in power costs are minimizing that benefit. The Environmental Services fund will present several opportunities for Council consideration. These include glass recycling, the environmental service fee and continuation of alternative daily cover at the landfill. Stormwater is still in the infant stage as a utility and continues with their work program to maintain compliance with federal storm water requirements.

#### Conclusion

In summary, this budget primarily maintains the existing programs and services while meeting commitments made by previous acquisitions, capital projects or program expansions. Our economic development efforts will be more important than ever as we attempt to mitigate any economic downturn in the Flagstaff economy. The State's budget woes will have a material impact on our budget and combined with a local revenue slowdown could even result in cuts during the subsequent fiscal year. Consequently, we need to be guided by caution in this upcoming year.

Despite these sour notes, we will see the fruit of much labor come on line as the Aquaplex opens, FUTS trails and open space are acquired, affordable housing units are constructed, and previously hired police personnel hit the streets with their training complete. We must keep in mind that the existing budget and personnel can and will continue to improve our community and make "Flagstaff a sustainable, safe and vibrant community retaining the character, high quality of life and charm of a small town."

Kevin Burke City Manager



# The City of Flagstaff Service At A Higher Elevation

# Mission

The Mission of the City of Flagstaff is to enhance the quality of life of its citizens while protecting the values of our community.

# Vision

The City of Flagstaff will be a sustainable, safe and vibrant community retaining the character, high quality of life and charm of a small town. Flagstaff will offer economic opportunities, educational choices, attainable housing, a protected environment and cultural and career opportunities to a diverse population

# **Values**

*Our Values*As employees we hold ourselves accountable to these values:

Accountability
We value accountability.

Responsiveness
We value addressing our customers' concerns.

Quality
We provide high-quality customer service

 ${\it Professionalism} \\ {\it We are honest, responsible, accountable, highly-trained, and cost conscious.}$ 

Teamwork
We are a team in partnership with citizens and other agencies for a better Flagstaff.

Problem Solving
We solve problems in a creative, open-minded, and professional manner.