



SPENDING CAP OVERVIEW

COMMISSIONER OF FINANCE

JOHN O'NEILL

TOWN OF BROOKHAVEN
TOWN BOARD WORK SESSION
APRIL 15, 2010

Introduction



- The growth in expenses and revenue decline of the Town's General Fund (A) is an area of fiscal concern.
 - ✓ Total annual expenses in 2002 were \$117.1 Million. For 2009, total annual expenses have increased to \$160.4 million (un-audited).
 - ✓ Over the last five completed fiscal years, 2005 thru 2009, 2007 is the only fiscal year the town was structurally balanced, i.e. did not need to apply surplus to balance. Simply put, expenses have outpaced revenue.
 - ✓ The application of surplus has led to an accelerating draw down of the General (A) Fund Balance. At year-end 2004, Fund Balance was \$82.6 million versus an estimated 2009 year-end (un-audited) fund balance of \$57.5 million.
 - ✓ 2010 General Fund Property Taxes are \$20.9 million (zero growth) with the tax rate held constant at \$4.47 per \$100 of assessed value.
 - ✓ Taking no action at the current run-rate will deplete the reserve before year end 2012 as per the MYP prepared by Munistat.

General Fund (A) Revenue has Decreased

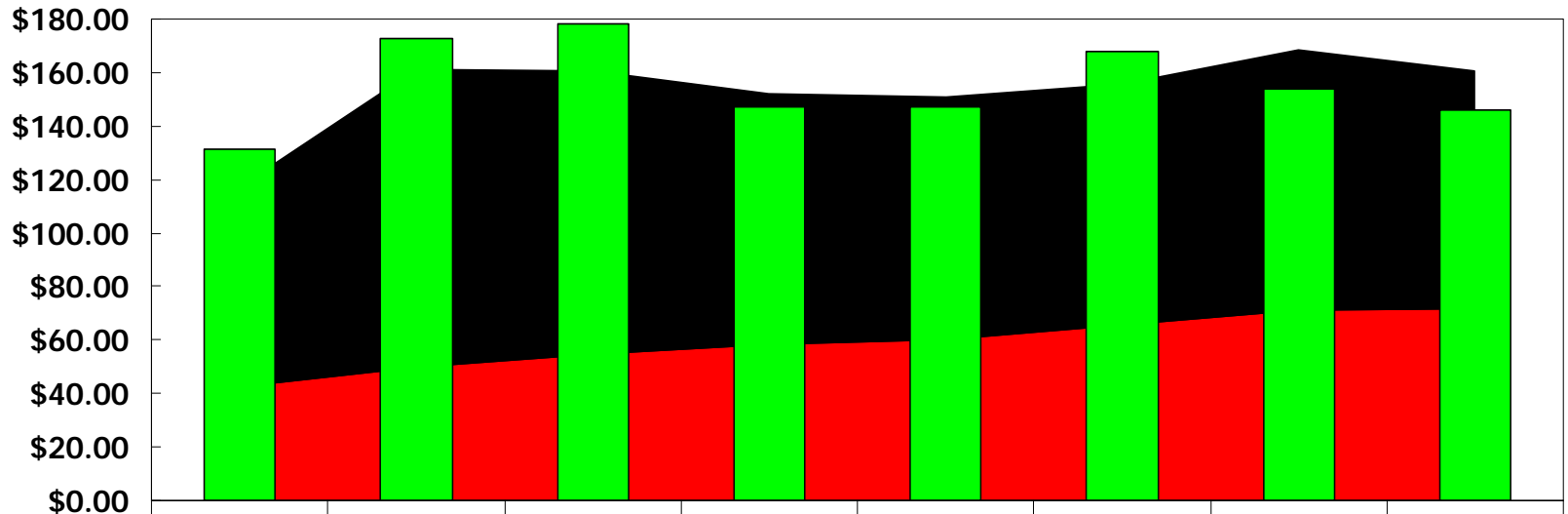


- There are three major drivers of revenue: Landfill Revenue, Mortgage tax and Property taxes. These “big three” drivers accounted for 77.3% (\$140.4 million) of total revenue in 2007, however the same big three drivers account for only 64.5% (\$97.5 million) in the 2010 budget.
 - ✓ Annual Landfill Revenue peaked in 2007 at \$89.9 million but has declined to \$66.6 million in the 2010 Budget.
 - ✓ Annual Mortgage Tax Revenue climbed to \$37.6 million in 2004. However, mortgage tax receipts have dropped dramatically to a budgeted level of only \$10.0 million for 2010.
 - ✓ Property Taxes: After tax holidays (i.e. \$0 collections) in 2005 & 2006, property taxes have been flat at about \$21 million.
- The continued reliance of the Town to use fund balance to plug the revenue gap has been exacerbated by an **INCREASE in expenses** over the corresponding time frame.

Revenue & Expense Trend: Historical Data



Total Revenue versus Total Expense
\$ Million



	2002 Act	2003 Act	2004 Act	2005 Act	2006 Act	2007 Act	2008 Act	2009 Esti.
■ All Other Expenses	\$74.54	\$111.57	\$106.21	\$93.57	\$90.71	\$89.78	\$97.44	\$88.84
■ Staffing (Sal. & Ben.)	\$42.86	\$49.64	\$54.62	\$58.47	\$60.12	\$65.81	\$70.95	\$71.54
■ Revenue	\$131.40	\$172.50	\$177.91	\$147.14	\$147.29	\$168.05	\$153.76	\$145.77

How are other municipalities coping?



- New York State has a \$9.2 Billion Gap and is growing each day....
- Suffolk County has stated for fiscal year 2010 the county is projecting a \$292.7 million gap of which \$140 million has been closed. The remaining gap is ~\$153 million, with some county legislators requesting a draw down on the Tax Stabilization Reserve Fund to partially offset the remaining gap.
- Bellport Village is proposing tax a tax increase.
- School districts such as Miller Place, Shoreham-Wading River, William Floyd and Three Village are proposing tax rate and levy increases and / or reducing services for their next budget.

Spending Caps



➤ Methodologies:

- ✓ The most common methodology is to anchor the spending based on the historical 3 or 4 year average growth in inflation, with the CPI-U the most common metric chosen.
- ✓ Another methodology employs a hybrid approach of a 3-year average CPI-U plus an adjustment for population growth.
- ✓ In NYS, multiple proposals have been debated:
 - Governor Paterson has proposed a cap of 4% or CPI, which ever is lower, on discretionary spending.
 - Another methodology employed is to use growth of 120% of prior year median income growth rate or some other revenue growth metric.

Municipalities with Spending Caps



➤ Spending Cap Considerations:

- ✓ In 1992 Colorado implemented a TABOR (Taxpayers Bill of Rights) Spending Cap formula based on population growth and inflation. Taxes that provided surpluses were returned to the taxpayers. This plan became controversial when the recession hit, as they were unable to add back to fund balance. This has since been amended to allow surpluses to be retained for 5 years to replenish fund balance.
- ✓ Maine implemented a spending cap in 2004. From 2004 through 2008, Maine expenses came in under their spending cap by \$221 million. Over the same time period, property taxes grew at an average rate of 3.9%. Prior to the spending cap property taxes grew at rate of more than 5 % per year.

What if the Town had a Spending Cap in 2002?



What If Analysis - Historical Expenditures versus Impact of Spending Cap in 2002

Year	Actual Expenditures	Expenditures w/cap	3 Yr. Avg. CPI Cap **	Excess/(Savings) over cap
2002	\$117,402,381	\$117,402,381	Base Year in Calculation	
2003	\$161,208,178	\$120,371,260	2.53%	\$40,836,918
2004	\$160,825,900	\$123,658,745	2.73%	\$37,167,155
2005	\$152,041,902	\$127,022,485	2.72%	\$25,019,417
2006	\$150,833,585	\$130,908,916	3.06%	\$19,924,669
2007	\$155,588,430	\$135,478,016	3.49%	\$20,110,414
2008	\$168,385,163	\$140,516,676	3.72%	\$27,868,487
2009	\$160,381,471	\$145,409,446	3.48%	\$14,972,025
Total Expenditures 2002 - 2009	\$1,226,667,010	\$1,040,767,925		\$185,899,085

**Consumer Price Index - All Urban Consumers

Series Id: CUURA101SA0, CUUSA101SA0

Not Seasonally Adjusted

Area: New York-Northern New Jersey-Long Island, NY-NJ-CT-PA

Item: All items

Base Period: 1982-84=100

Spending Cap Strategy:



- **Implement a reasonable spending cap or a cost containment strategy that is both meaningful and flexible for the taxpayers of the Town.** The strategy should work in concert with the fiscal policies of the town (i.e. debt management policy & fund balance policy).
- **Be flexible**, exceptions can be made by super majority for emergencies or projects that will pay for themselves. Meaning, revenue collected must outpace total project cost including debt service.
- **Expense amendments should be “PAYGO”, Pay-As-You-Go.** Any amendments, i.e. additional expenditures to the capital or operating budget, must be budget neutral. For every increase there must be at least an equal and offsetting decrease.
- **Control Capital Spending**, back into the next years capital budget by determining how much debt service the town can afford to get into compliance with the current debt policy by year end 2015.
- **Rating agencies frown upon tax caps** and a municipality can be downgraded if one is implemented. Rating agencies do not want a predictable revenue stream to be constrained in any way should an emergency arise. For example, the Town’s positive outlook was removed in 2005 when a second property tax holiday was implemented.

Spending Cap Options



- Implement a spending cap. However, until the Town's budget is structurally balanced, the Town should be reducing expenses not growing spending.
- 1. Three Year CPI-U Annual Average Growth Rate - Least Restrictive:**
 - Pros - easily to calculate, currently in use and a three-year average will smooth the peaks and valleys of year to year spikes.
 - Cons - CPI-U is not representative of what a municipality purchases or the ability to re-pay. Allows expenses to grow too fast in the good times.
 - 2. Three Year Population Growth Rate - Most restrictive:**
 - Pros - easily to calculate, will smooth the peaks and valleys of year to year spikes and is representative of what is happening locally in the town.
 - Cons - There are different reasons for slow population growth. For example, economic recession or taxes too high. Does not take into account inflation.
 - ★ 3. Three Year Average of Revenue Growth plus Three Year Average Population Growth Rate - Restrictive yet flexible:**
 - **Once structurally balanced, 50% of the excess surplus each year can be set aside to reduce debt service, fund capital projects, fund open space preservation, or reduce taxes - Restrictive yet flexible**
 - Pros - Pegs expense growth to revenue growth- the ability to re-pay, population growth partially accounts for expenses and a three year average will smooth the peaks and valleys of year to year spikes.
 - Cons - does not directly account for inflation and requires additional calculations.

Appendix:



CPI-Definition



What is the CPI?

The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services.

How is the CPI market basket determined?

The CPI market basket is developed from detailed expenditure information provided by families and individuals on what they actually bought. For the current CPI, this information was collected from the Consumer Expenditure Surveys for 2005 and 2006. In each of those years, about 7,000 families from around the country provided information each quarter on their spending habits in the interview survey. To collect information on frequently purchased items, such as food and personal care products, another 7,000 families in each of these years kept diaries listing everything they bought during a 2-week period.

CPI-U- Definition



What is the CPI-U?

The all urban consumer group represents about 87 percent of the total U.S. population. It is based on the expenditures of almost all residents of urban or metropolitan areas, including professionals, the self-employed, the poor, the unemployed, and retired people, as well as urban wage earners and clerical workers.

Not included in the CPI are the spending patterns of people living in rural Non-metropolitan areas, farm families, people in the Armed Forces, and those in institutions, such as prisons and mental hospitals.

Consumer inflation for all urban consumers is measured by two indexes, namely, the Consumer Price Index for All Urban Consumers (CPI-U) and the Chained Consumer Price Index for All Urban Consumers (C-CPI-U). "

Municipalities with Spending Caps



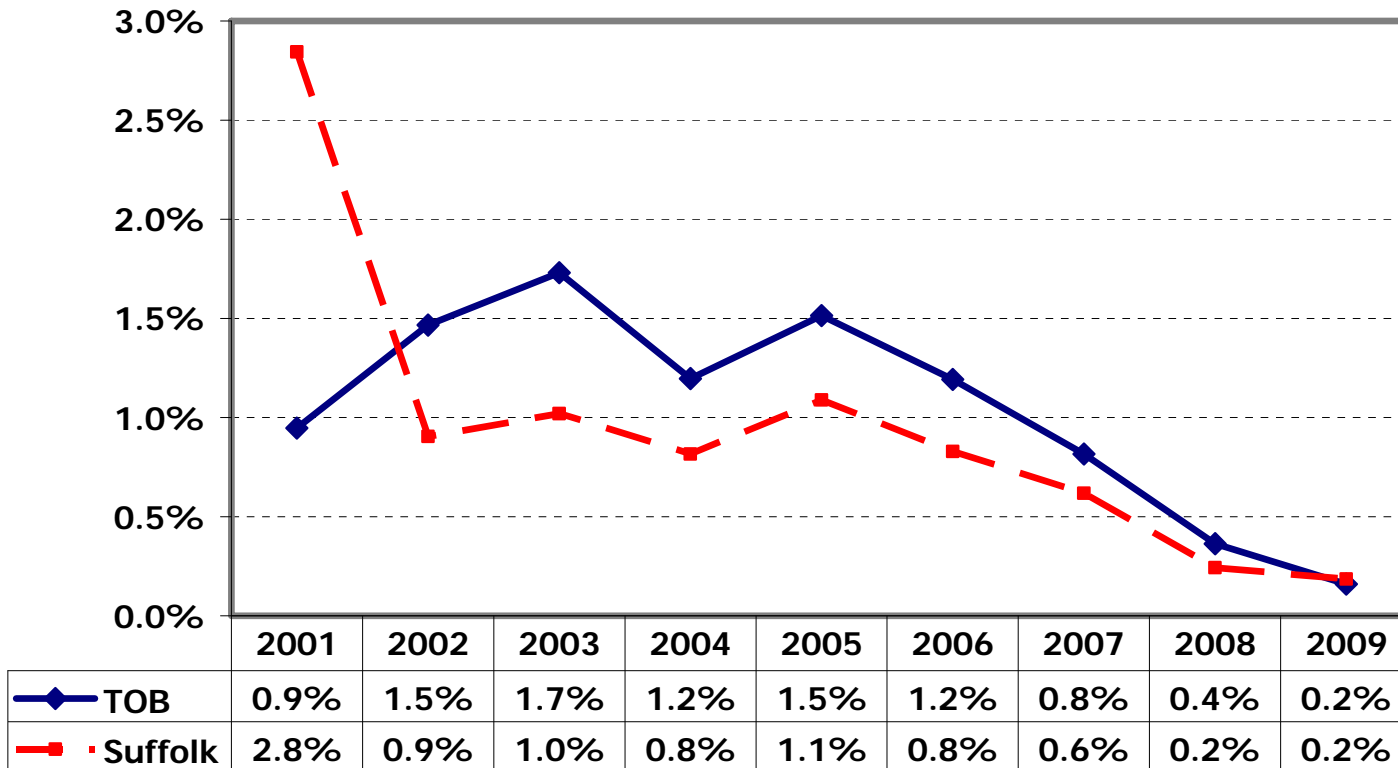
➤ Additional Spending Cap Considerations:

- ✓ City of Norwalk, CT had a spending cap based on the CPI-U and ran into a problem in 2006, when department budget submissions exceeded the cap. Since the council adopted a budget in excess of the spending cap, property taxes were increased.
- ✓ Washington D.C. implemented a Debt Service cap of 12% in the summer of 2008 after their debt service reached 17%. The CFO for D.C., Dr. Gandhi, cited the negative impact to D.C.'s credit rating with such high debt levels. Dr. Gandhi noted "For the State of Maryland, Debt Service cannot exceed 8% of revenue for Virginia it the limit is 5%." Dr. Gandhi recommended "a cap of 12% and a goal of 10%. When Debt Service exceeds 10% of total expenditures it is a "red flag" for credit agencies."

Annual Population Growth Town versus County



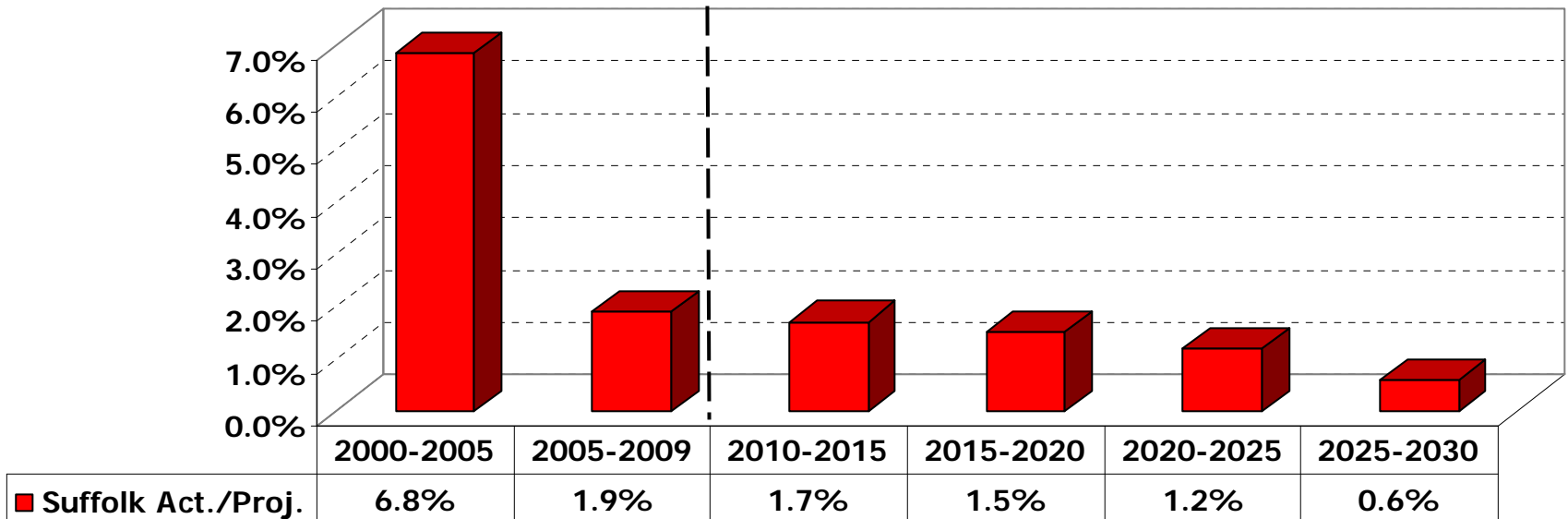
LIPA Annual Survey - Population Growth Estimate



Suffolk County Population



Population Suffolk County Growth &
NYS DOL Projection



What if the Town had a Spending Cap in 2002-Normalized



What If Analysis - Historical Expenditures versus Impact of Spending Cap in 2002

Year	Actual Expenditures	Expenditures w/cap	3 Yr. Avg. CPI Cap **	Excess/(Savings) over cap
2002*	\$141,802,381	\$141,802,381	Base Year in Calculation	
2003	\$161,208,178	\$145,388,288	2.53%	\$15,819,890
2004	\$160,825,900	\$149,359,019	2.73%	\$11,466,881
2005	\$152,041,902	\$153,421,853	2.72%	-\$1,379,951
2006	\$150,833,585	\$158,116,009	3.06%	-\$7,282,424
2007	\$155,588,430	\$163,634,715	3.49%	-\$8,046,285
2008	\$168,385,163	\$169,720,572	3.72%	-\$1,335,409
2009	\$160,381,471	\$175,630,217	3.48%	-\$15,248,746
Total Expenditures 2002 - 2009	\$1,251,067,010	\$1,257,073,055		-\$6,006,045

*2002 Actual Increased \$24.4M, normalized for the following 2003 unique items: Land Donation Golf Course \$12.9m, Debt Service Transfer Medford Complex \$9.5M, Seniors Div. B Fund transfer \$1.0M & Retirement Rate change \$1.0M.

**Consumer Price Index - All Urban Consumers

Series Id: CUURA101SA0,CUUSA101SA0

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Item: All items

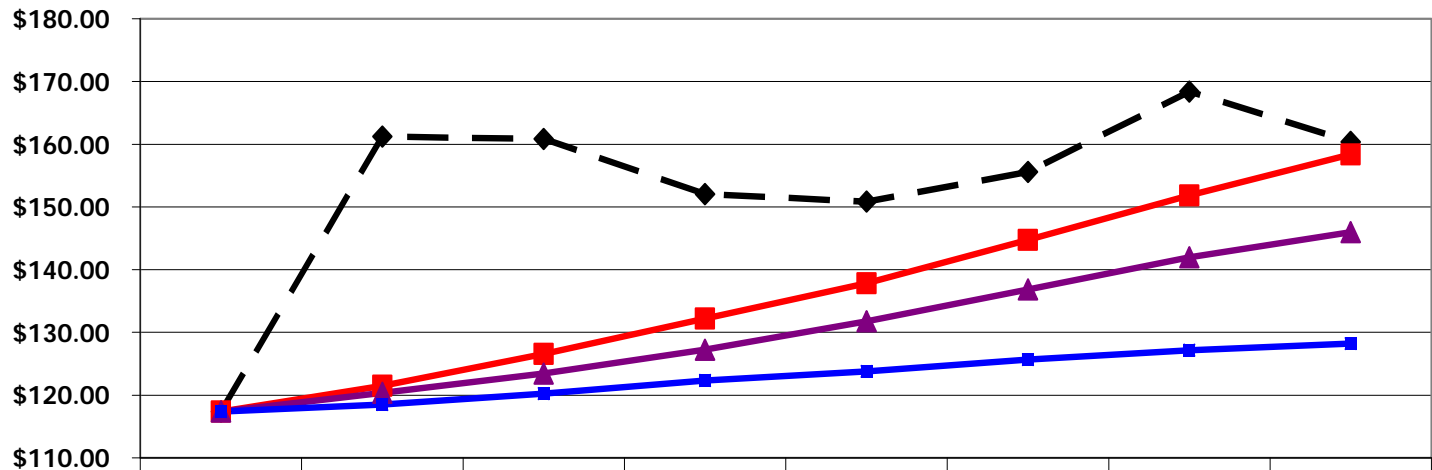
Base Period: 1982-84=100

What if the Town had a Spending Cap in 2002?



ACTUAL TOTAL EXPENSE GROWTH VERUS EXPENSE CAP WITH 2002 AS A BASE

\$ in Millions



	2002	2003	2004	2005	2006	2007	2008	2009
Actual - Total Expenses	\$117.40	\$161.21	\$160.83	\$152.04	\$150.83	\$155.59	\$168.39	\$160.38
Cap - CPI 3 Yr. Avg. + Pop.	\$117.40	\$121.48	\$126.58	\$132.21	\$137.84	\$144.74	\$151.85	\$158.38
Cap - CPI Annual only	\$117.40	\$120.36	\$123.45	\$127.24	\$131.75	\$136.83	\$141.98	\$145.99
Cap - Population Only	\$117.40	\$118.51	\$120.25	\$122.33	\$123.80	\$125.67	\$127.17	\$128.21

Proposed Debt Control & Capital Budget Policies

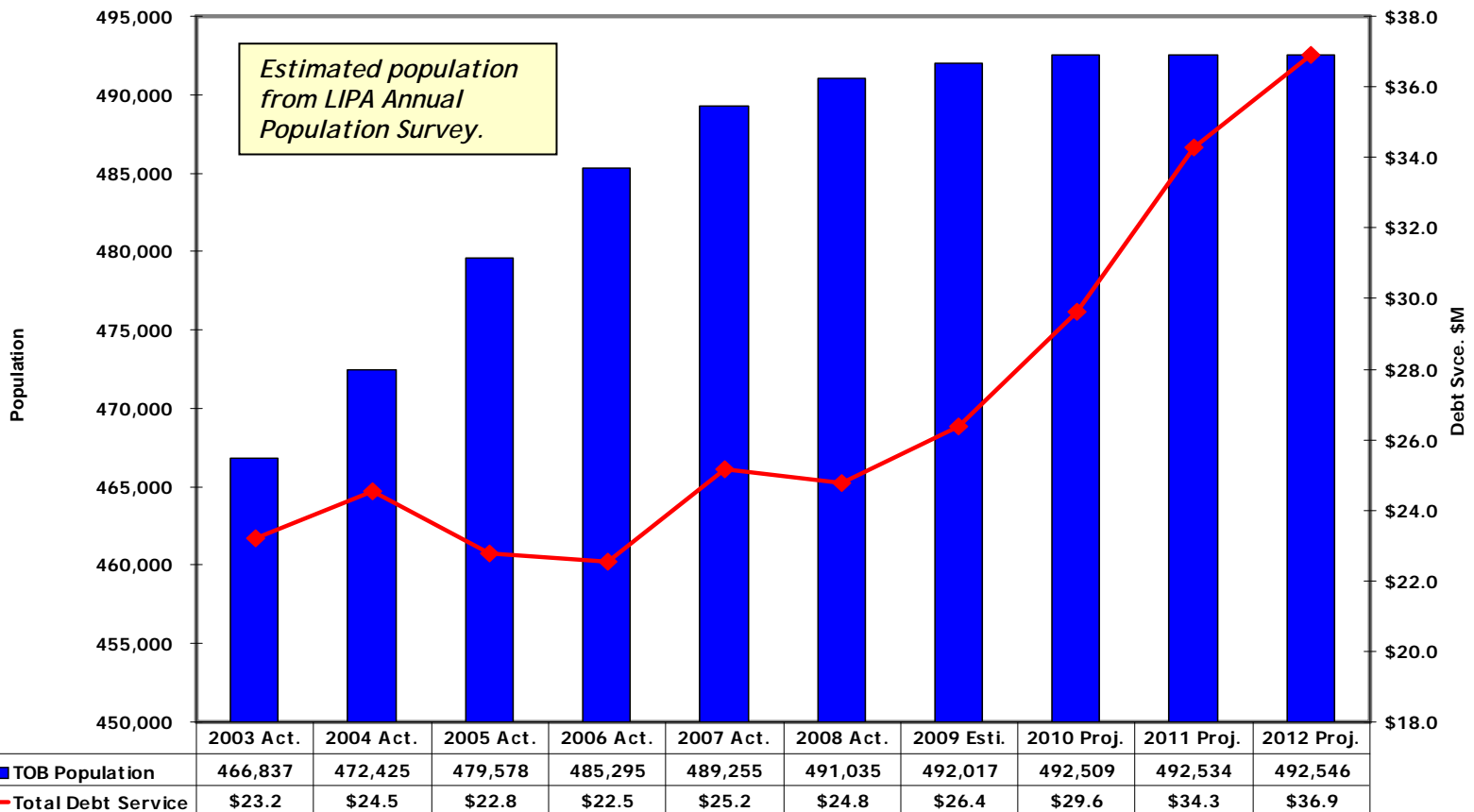


- General Fund Debt Service should be no more than 15% of the lesser of:
 - ✓ revenues (excluding any application of surplus), or
 - ✓ expenditures.
- The Capital Budget is fixed in terms of overall dollars. If any new projects are added during the fiscal year, other project(s) must be deferred to maintain the fixed dollar capital budget limit.
- Conduct a needs assessment of the Town's capital assets and infrastructure to identify the most critical construction and reconstruction needs. This would be the basis for the Town's 5-year capital plan and allow the Town Board to prioritize capital project investments, identify critical infrastructure needs and ensure that the Town's limited debt capacity is used effectively.

Debt Service: Compared to Town Population



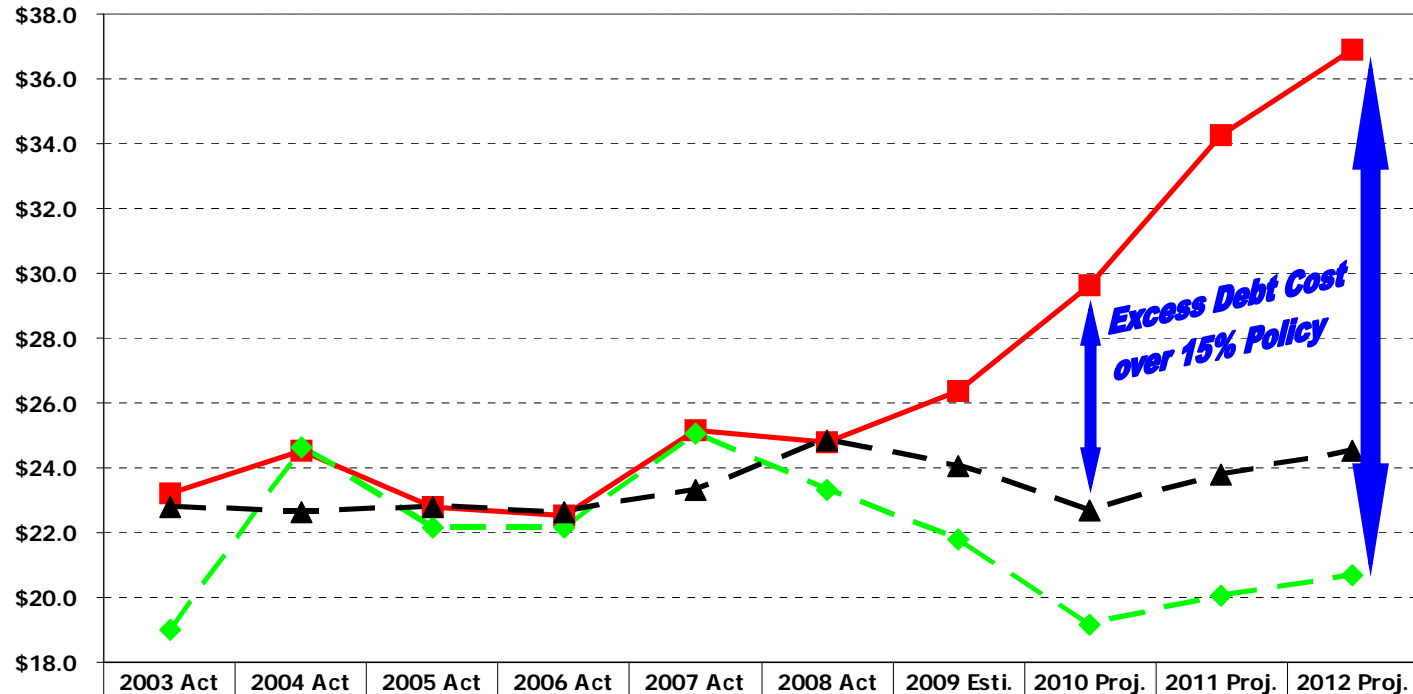
Debt Service versus Population



Debt Service: Current vs. Proposed Policy



Annual Debt Service Trend with Target
General Fund A - Town Wide Only



■ Total Debt Svce.	\$23.2	\$24.5	\$22.8	\$22.5	\$25.2	\$24.8	\$26.4	\$29.6	\$34.3	\$36.9
◆ Target 15% of Rev.	\$19.0	\$24.6	\$22.2	\$22.1	\$25.0	\$23.3	\$21.8	\$19.1	\$20.1	\$20.7
▲ Target 15% of Exp	\$22.8	\$22.6	\$22.8	\$22.6	\$23.3	\$24.9	\$24.1	\$22.7	\$23.8	\$24.5