REPORT TO THE ANCHORAGE ASSEMBLY

NOVEMBER 18, 2009

OFFICE OF THE MUNICIPAL ATTORNEY

INTRODUCTION:

The Assembly retained the firm Walker & Levesque, LLC to render an opinion ("Levesque opinion") on the "conditions precedent to valid Assembly action in the ratification of labor agreements."[1] The Levesque opinion, dated September 23, 2009, specifically addresses the validity of two Collective Bargaining Agreements (CBAs) approved by the Assembly in December of 2008.[2]

Pursuant to AR 2009-241, approved September 29, 2009, this office has been asked to review the Levesque opinion, as well as a subsequent letter from the IAFF regarding the validity of its agreement[3], and render an assessment of the validity of the labor agreements and related issues surrounding the process by which the agreements were approved.[4] This report constitutes our review and analysis of the issues presented.

BACKGROUND:

We start with a brief history of events, starting with the following table regarding the Assembly's approval of labor agreements during 2008.

Contract	Approved	Term of agreement	Revisited by the Assembly after January 1, 2009	Assembly Action on items revisited
Local 959 (Teamsters)	2/26/2008	3 year, 4 month	5/12/2009 - AR 2009-115 (wage concessions)	Approved.
Local 71 (Public employees)	8/12/2008	5 year	7/21/2009 – AR 2009-163 (wage concessions)	Approved.
Local 302 (Operating Engineers)	10/14/2008 AR 2008-186	5 years	6/16/2009 – AR 2009-132 (wage concessions with two year extension)	Failed.
AMEA	12/2/2008 AR 2008-266	5 years	2/24/2009 – AR 2009-22 (corrections) 6/16/2009 – AR 2009-146 (wage concessions)	Approved. Approved.
IBEW	12/2/2008 AR 2009-280	5 years	2/24/2009 – Notices by Coffey and Johnston 3/3/2009 – AR 2009-63 (rescission) **AR 2009-280 carried over to 3/24/2009**	 Failed.
APDEA	12/16/2008 AR 2009-307	5 years	1/30/2009 – AR 2009-12 and AR 2009-13 2/24/2009 – Notices by Starr and Johnston 3/24/2009 - AR 2009-66 5/26/2009 – AR 2009-133 (wage concessions) **AR 2009-307 carried over to 3/24/2009**	Approved. Postponed indefinitely 6/9/2009 Approved.

[1] AR 2009-77(S) (March 24, 2009).
[2] AR 2008-280 (December 2, 2008)(IBEW) and AR 2008-307 (December 16, 2008)(APDEA).
[3] Anchorage Firefighters Local 1264 letter dated September 29, 2009, with cover letter from Jermain, Dunnagan & Owens, P.C. The Assembly approved the IAFF agreement on December 17, 2009 (AR 2009-306).
[4] AR 2009-241 provides "The Administration, through the Department of Law, is requested to review and analyze the Levesque report dated September 23, 2009, to include an examination of the facts and the law associated with both the report and the questions asked in AR 2009-77(S) and all other information, reports, [and] analysis relevant to the issue, including legal opinions from any available source, including the Jermain Dunnagan & Owens, P.C. report, and make a written report to the Assembly no later than November 15, 2009."

IAFF	12/17/2008 AR 2009-306	5 years	2/24/2009 – Notice by Johnston 4/14/2009 – AR 2009-85 (wage concessions) **AR 2009-306 carried over to 3/24/2009**	No Action. Approved.

The table shows that the labor agreements are all 5 year agreements, with one exception. The table also shows that each contract was revisited and subsequently amended by the Assembly in the late spring or early summer of 2009, with two exceptions – the Local 302 contract and the IBEW contract.

Over the course of 2008, the national economy deteriorated. Our review of the Assembly minutes from meetings and work sessions between August and December of 2008 make it clear that the Assembly and the Begich Administration were well aware of the national economic trends during this time period. It is also clear that both branches of government understood that the national trends were having some effect on local government tax revenue and earnings on investments, primarily related to decreases in vehicle rental tax and hotel\motel bed tax on the tax revenue side, and decreases in the value of holdings in financial markets on the investments side, for both the cash pools and the MOA Trust Fund. The economy also was having an effect on the bond market, threatening the Municipality's ability to borrow.

With this general knowledge of both the state of the national economy and its impact on local government revenue, the Assembly, on November 25, 2008, approved the second half of its biennial budget, covering 2009.[5] This budget included $7 million from the MOA Trust Fund and the anticipation of approximately $15 million in state revenue sharing funds to be used for property tax relief.

Then, in December, 2008 the Assembly approved four of the collective bargaining agreements listed in the above table. In between the approval of two of the contracts on December 2 and the approval of two more on December 16 and 17, CFO Weddleton sent two emails to Mayor Begich that contained a spreadsheet of Budget Risk Factors that indicated her "best guess estimate" of approximately $33 million dollars in risks.[6]

In January of 2009, the Claman Administration advised the Assembly that the 2009 budget, just adopted in November of 2008, would be short on the revenue side by approximately $17 million. Some Assembly members moved to rescind or modify their approval of two of the CBAs on grounds that the Assembly was not adequately advised of the financial status of the Municipality at the time the CBAs were approved and that there were other defects with respect to the CBAs, including the adequacy of the Summary of Economic Effects, presentation of final versions at the time of approval, and terms within the CBAs.

[5] AO 2008-102(S) as amended.

[6] Weddleton to Begich emails, December 9, 2008. The first email, widely distributed in response to public records requests, indicates that November investment returns were "horrible" and proposes some stop-gap measures, including a hiring freeze and cessation of discretionary spending. "Additionally, a relatively new issue is that departments (not only Fire) have started blowing their budgets several weeks earlier in the year than normal. We can "cosmetically" make it look like they're adhering to their budgets by reversing the PERS for 7/08 to 12/08 but the related state "revenues" disappear, too, so this means that their spending is exceeding their revenues." The second email only contains a revised spreadsheet that includes Cooperative Services Authority (CSA), adding $1,269,990 to the "best guess estimate", bringing the total to just over $33 million.

A significant amount of attention has focused on the availability of a remedy – rescission of the CBAs. But, there is no reason to discuss remedies unless we first determine whether there is some basis to trigger invocation of a remedy.

ISSUES PRESENTED:

A. Whether former Mayor Begich violated Anchorage Municipal Charter §13.06(a) by failing to report that revenues were projected to be less than appropriations for the fiscal year and, if so, what legal consequences or remedies flow from this violation, including whether the CBAs can be rescinded.

B. Notwithstanding whether Mayor Begich violated Anchorage Municipal Charter §13.06(a), is there a legal basis to find the CBAs invalid or upon which to rescind them?

Discussion: Whether former Mayor Begich violated Anchorage Municipal Charter §13.06(a)

A. Charter / Code History

Adopted in 1975, Anchorage Municipal Charter §13.06(a) provides, in pertinent part:

> If the mayor determines that revenues will be less than appropriations for a fiscal year, the mayor shall so report to the assembly.

The quoted language of Charter §13.06(a) is similar to language present in two prior, unratified versions of the Charter from 1970 and 1971. Both prior versions read as follows (emphasis added):

> If the mayor determines that revenues will be less than appropriations for a fiscal year, the mayor shall so report to the assembly *without delay*.

The Charter language ultimately adopted did not include the phrase "without delay" and is not specifically addressed in the Charter Commission Commentary. Nor is it addressed in the Charter Commission minutes.[7] Nevertheless, the Commission meetings were recorded and there is a short conversation amongst the Commission members on this sentence. In the conversation, they are discussing the section at issue, which is the "first sentence" in the dialogue below:

> Speaker 1: Why don't we stick with (a) for a minute…
>
> Speaker 2: Ok, let's stick with (a), alright. I, I jumped all out of context here…

[7] Anchorage Municipal Code at section 6.10.090, which implemented the Charter provision, simply mimicked the Charter's language and was later removed.

Speaker 3: The reason, in my report, I said that the committee only felt the second sentence was unnecessary, was that some members of the committee felt the first sentence can get usefulness. That is, if the mayor determines the revenues would be less than appropriations for the fiscal year that the assembly should get the **early warning signal** and not.... and he should be obligated by charter to bring that to…

Speaker 2: Give the **early warning signal**, not wait until it happened if he knew about it is gonna happen ahead of time.[8]

While helpful, a brief expression of intent like this is not determinative; it is informative. We turn, then, to the code provisions in effect before and at unification to see if they better inform an understanding of either the Charter provision or how it was implemented through code. Before and at unification, the Greater Anchorage Area Borough code provided:

> The Mayor of the Borough shall make monthly reports to the Assembly on Borough finances and operations. (Refer to AS 29.23.140(g).) The monthly reports shall be rendered in condensed format and will include current and year-to-date financial information.[9]

The City of Anchorage Charter provided:

> The city manager shall submit periodically to the council information comparing estimated and actual revenues and expenditures to the end of the preceding month.[10]

Before and at the time of unification, AS 29.23.140 and AS 29.23.290 provided[11]:

> **AS 29.23.140 Powers and Duties of Borough Administrator.** The borough mayor or manager as the case may be, as the chief administrative officer, is responsible for the proper administration of all borough affairs. The mayor or manager of the borough shall
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> * * *
>
> (6) make monthly reports to the assembly on borough finances and operations,

> **AS 29.23.290 Powers and Duties of City Manager.** If the city has a manager, he is the chief administrative officer. The manager shall
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> * * *
>
> (6) make monthly reports to the council on city finances and operations;

At the time of unification, the two above statutory provisions no longer applied because AS 29.13.100, which contained the list of mandatory statutory provisions applicable to home rule municipalities, did not include either of the above, or any other statutory requirement, for monthly financial reporting. However, the underlying GAAB and City of Anchorage provisions still applied to the newly formed Municipality of Anchorage, pursuant to Charter §19.05.

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[8] July 1, 1975 Charter Commission meeting.
[9] OR-74-127.
[10] City of Anchorage Charter § 6.4(b).
[11] These statutes were later combined into AS 29.20.500 (§7 ch 74 SLA 1985).

The Assembly then approved AO 248-76A on November 23, 1976, which included adoption of AMC section 6.40.010, which stated:

> The mayor shall make reports to the Assembly on municipal finances and operations. The monthly reports shall be rendered in condensed format and will include current and year-to-date financial information.

This section of the Code now reads:

> The chief fiscal officer shall install and have supervision over the accounts of all organizational elements of the municipality. Such accounts shall show in detail the financial transactions of all departments. **The chief fiscal officer shall cause a monthly statement, in condensed format, to be prepared and distributed to the assembly, the mayor and all department heads, showing the aggregate revenues and expenditures of each fund of the municipality for the preceding month as well as the year-to-date accumulative amount.** (emphasis added)

A reasonable read of what is expected by the Code to be in a year-to-date analysis would be a comparison of budgeted revenues to actual revenues for the specified time periods, which are monthly and year-to-date, but does not expressly include a year-end revenue projection. Restated, the current Code section does not expressly require reporting of the fiscal year-end revenue shortfall forecast described in the Charter provision.[12] Current Code does not implement or further define the Charter provision at issue.

B. Applicable standards, in the absence of express provisions

What triggers the requirement to report to the Assembly?

1. Reasonable certainty of a revenue shortfall

In the absence of a Code provision implementing the Charter provision, we must determine its meaning using general rules of construction.[13] These include reading all parts together, considering the intention of the framers, and giving plain meaning to undefined terms.[14] Utilizing these rules, we turn to consideration of what triggers the Charter requirement to report. The Charter states that the report is required when revenues "will be" less than appropriations. This raises the issue as to what level of certainty is required before it can be said that revenues "will be" less than appropriations and then must be reported. The word "will" is, in comparison with the word "may", a word of certainty, not one of speculation.[15] It is also a word of probability.[16] In the context of managing budgets, the certainty need not be absolute; still, it is something more than a mere possibility. Absolute certainty in budgeting may not come until the

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[12] Only the City of Anchorage Charter expressly required "information comparing estimated and actual revenues and expenditures to the end of the preceding month" but this is not a requirement to report a fiscal year-end projection.
[13] McQuillan, *Municipal Corporations*, §9.22.
[14] Id.
[15] Webster's II New Riverside University Dictionary, 1988.
[16] Id.

books for the fiscal year are closed the following spring. Likewise, a mere possibility may result in frequent, alarmist or unreliable reports. In between these two extremes is a standard of reasonableness. If the shortfall is anticipated with a reasonable certainty, it should be reported. Waiting for absolute certainty would appear to be far too late to take advantage of many opportunities to adjust spending. Waiting for absolute certainty would tend to negate the very next sentence in the Charter, which provides "The assembly may reduce appropriations as it deems necessary."

Our "reasonable certainty" standard is not unassailable. Like many such standards or doctrines, including "reasonable doubt", "reasonable care", "reasonable person", and "reasonable time", it is itself going to be subject to disagreement, between reasonable minds, as to whether any particular facts meet the standard. Yet, we must give meaning to the Charter provision and a method of implementing that meaning.

2. Amount of a revenue shortfall

Part of the equation should also consider the amount of the shortfall and not just its certainty. The 100% certainty the Municipality is $1 short on revenue is not as important as the 50% certainty the Municipality will be $10 million short on revenue. This is one of those areas where an arbitrary standard is often applied, such as requiring a shortfall of greater than 1% of budgeted revenue be reported, for instance. In the absence of such an express standard, we derive the standard should be one that considers the circumstances and determines whether the circumstances justify, or obligate, reporting: Is the projected revenue shortfall significant, given the circumstances?[17]

How often should determinations be made?

The Mayor has an ongoing obligation to make determinations about revenues in comparison with the budget, including projections regarding anticipated revenue. This is inherent in the nature of the obligation to administer the budget. However, we acknowledge neither the Charter nor the Code quantify this obligation. For purposes of this report we do not need to further quantify the obligation; we find the Begich Administration met or exceeded the obligation to make ongoing determinations. For many years, the Begich Administration engaged in an ongoing process of projecting year-end revenues against budgeted revenues.

When and how should the report be made to the Assembly?

In the absence of additional legislative intent or implementation through Code provisions, this Office is of the opinion the reporting anticipated by the Charter provision should be timely, giving consideration to the severity of the shortfall and its risks to the stability of municipal finances, including the possibility or probability of the need to trim expenditures or utilize fund balance.[18] If monthly reporting of revenues to date is required by Code, we see no reason why,

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[17] Again, we acknowledge that this standard, like the one discussed previously, is not unassailable.

[18] The Assembly could give further guidance in this area, if it chooses. At the time of this report there are proposals before the Assembly on the subject.

once a determination that revenues will be less than appropriations for the fiscal year is made, as anticipated by the Charter, it should not be reported to the Assembly at its next regularly scheduled meeting, but certainly in conjunction with the monthly reporting already required by Code. Since the method of reporting is unspecified in the Charter, an Assembly Information Memorandum (AIM) is adequate, but even a verbal presentation through the Mayor's Report agenda item available at every meeting would suffice, as would a memorandum delivered to the Clerk's Office. Monthly reporting, starting with data from the end of May, will give the Assembly more time to adjust appropriations in the budget should it choose to do so, and would meet the "early warning" described by the Charter Commission.

C. Did Mayor Begich know, to a reasonable certainty, that revenues would be less than appropriations for the fiscal year 2008?

1. When did he know?

Mayor Begich may have had some indication as early as June 11, 2008 that revenues were a potential problem area and might be significantly below appropriations. In an email to the Mayor, the Municipal Manager, the OMB Director, and others, CFO Weddleton said the following regarding cash pool short term interest earnings:

> Effective immediately, the Controller Division should reject any PACE document that cites interest income from the short term cash pool and/or unrealized gains as a source of revenue for a proposed project. Please forward this e-mail to any individual who certs funds for PACE documents.
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> Background
> **Before the MOA changed its investment practices, it invested in very short term, low risk US Treasury and Agency securities. Though this offered an advantage of very low volatility, it came at the cost of extremely low yields.** The MOA had traditionally allocated interest and realized gains/losses to the cash pool participants every month, but had not allocated any (minor) unrealized gains/losses until year end.
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> **Recently, the MOA has fundamentally changed its investment practices to increase yields. A more aggressive approach has been implemented, but the result has been more volatility from month-to-month.** The MOA has maintained its traditional accounting allocation of only interest and realized gains/losses to the cash pool participants every month.
>
> Current Status
> **Unfortunately, the MOA currently has a significant unrealized loss. If booked, it would wipe out approximately 60% of our year-to-date interest and realized gains/losses. Therefore, we should not allow departments to spend their interest as it is effectively much lower than PeopleSoft would indicate.**

> We are contemplating a new policy which would allocate unrealized losses during the year. In the mean time, please reject any PACE items that cite unrealized gains and/or cash pool short term interest as a source of funds.[19]

If not in June, then Mayor Begich reasonably should have known to have known as early as July 8, 2008 that the revenues for 2008 were reasonably certain to be less than appropriations. This is the date Treasury presented the first of a series of reports for 2008 entitled “Analysis of General Government Revenues” (“July Report”) to what was then called the Executive Committee. The Executive Committee was comprised of three members of Treasury, OMB Director, the Chief Fiscal Officer, the Municipal Manager, and the Economic and Community Development Executive Director.

The analysis reported to the Executive Committee contained detailed information on forecasted revenues compared to budgeted revenues for the same time period. The analysis was part of an ongoing reporting process started years earlier. The reports were prepared by Treasury staff hired specifically for the purpose of revenue forecasting and had achieved a high level of quality and accuracy over the course of their development. Generally, the reports were done each year, starting after the end of May, when reasonably useful incoming revenue data would be posted in PeopleSoft. These reports would be presented to the Executive Committee each month thereafter through the end of the year, with the exception of the report for data as of August 31, of each year because that report would have to be compiled and presented in October, at a time when it was difficult to get staff and the committee together due to budget preparation and other matters. “As of August 31” reports were not done for the years 2006, 2007, and 2008.

The July 2008 report, for the period ending May 31, 2008, clearly says “As of 7/7/08, our analysis shows a projected total general government revenue shortfall of ($7.1M) (1.3%) compared to 2008 budgeted revenues excluding Fund 181.”[20] The July Report also says “The revenue variance for Fund 181 is about negative ($3.5M)(39%).”[21] This brings the total variance between budgeted revenues and projected revenues for 2008 to $10.6 million, using data then available to the Municipality.

There were four more reports issued between August and December of 2008. The variance between projected revenues and budgeted revenues ran as follows:

	As of 5/31 Reported 7/8	As of 6/30 Reported 8/11	As of 7/31 Reported 9/23	As of 9/30 Reported 11/18	As of 10/31 Reported 12/17
All funds, except Building Safety	($7.1 Million)	($4.9 Million)	($4.9 Million)	($5 Million)	($7.9 Million)
Building Safety	($3.3 Million)	($3.2 Million)	($3.3 Million)	($2.8 Million)	($3.3 Million)
Total	($10.4 Million)	($8.1 Million)	($8.2 Million)	($7.8 Million)	($11.2 Million)

Recall that this data does not include expenditures over the 2008 budget that arose between each of the relevant reporting periods (fund balance spending). In the absence of another funding

[19] Weddleton to Begich email , dated June 11, 2008. (emphasis added)
[20] July Report, page 4. Fund 181 is Building Safety.
[21] Id.

source, expenditures over the 2008 budget would necessarily need to be "paid" out of fund balance. We discuss fund balance in more detail below.

2. Did Mayor Begich timely report the projected 2008 revenue shortfall to the Assembly?

We have no evidence the revenue analysis reports prepared by Treasury were shared with the Assembly at any time between June, 2008 and the end of December, 2008. We have no evidence the revenue shortfall projections contained in the reports were shared with the Assembly. CFO Weddleton did present a portion of this information regarding investment revenues to the Assembly at the October 17, 2008 work session. But, investment revenues are only a portion of the total revenue picture.

As of early October, 2008, the latest projection by Treasury indicated the Municipality would be $4.9 million under budgeted revenues, according to the "Analysis of General Government Revenues as of 7/31/08", of which $1.1 million was due to a decrease in interest revenue and another $1.4 million was from a decision to remove certain unrealized gains from interest earnings.

While CFO Weddleton and Mayor Begich have recently repeatedly referred to the October 17 work session as a critical meeting at which the Assembly received the bad news about municipal finances listed in the risk factors spreadsheet,[22] a close examination of that work session does not support their assertion, in as much as the work session did not cover the revenue shortfall for 2008 discussed above.

We asked Mayor Begich, "When did you first know to a reasonable certainty that projected revenue for fiscal year 2008 would not meet the budgeted revenue for fiscal year 2008?"[23]

He responded:

> It is difficult to know with any "reasonable certainty" how the fiscal year will balance out until the 13 or 14th month of the fiscal year. However, as we did throughout my terms as mayor, my administration closely monitored economic events that may have some bearing on city finances. That was especially true in late 2008, as other cities across the country began reporting serious fiscal challenges. Although Anchorage was in better fiscal shape than many cities, we communicated our concerns to the Assembly at the October 17, 2008 work session. This report included the stock market crash (which affects the MOA Trust Fund dividend), the flight to quality (which affected the carrying values on the Municipality's investments), investment losses that were considered to be permanent, and interest revenues. This work session was supplemented by other work sessions, committee meetings and reports (such as investment reports) that were provided to the Assembly. Of more than 60 Assembly work

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[22] Weddleton to Coffey email, January 20, 2009.
[23] Q&A exchange with Begich, November 14, 2009.

sessions held in 2008, at least a dozen were devoted to the state of city finances.[24]

We reviewed the work session materials and recording, and compared them with the Budget risk factor spreadsheet. The October 17 work session did not cover the projected shortfall in hotel\motel bed tax for fiscal year 2008 (item #1 on Risk Factor spreadsheet, $3 million). The work session did not adequately cover 2008 investment losses to the GCP (General Cash Pool)(item #2 on the spreadsheet, $5 million). To the extent it was discussed the GCP, the losses were minimized to a "real" number of $1.6 million. The work session presentation on unrealized and realized losses in cash pool investments did not address this in the context of the 2008 budget or whether 2009 earnings on the investment portfolio would be lower than budgeted (as proposed in the then pending 2009 budget)(item #11 on the spreadsheet, $3 million) The work session did not cover 2008 TANs losses (item #4 on the spreadsheet, $600,000), although it did cover the probability that selling TANs in 2009 would likely lose money). According to CFO Weddleton's "Best Guess Estimate", these items alone totaled $11.6 million. Yet, there was no suggestion from the Administration to the Assembly at the October 17 work session that 2008 revenues were reasonably certain to be under 2008 appropriations.

Reliance on the October 17 work session for the proposition that the Assembly was fully informed is misplaced for the above reason, but more importantly, financial information is not static.[25] We know the markets got worse after October 17, not better. What happened to the markets in October was even worse than the end of September data relied on at the October 17 work session. And, as CFO Weddleton herself has said, November was "horrible."[26] Thus, what the Assembly was told in mid-October is, by the first week of December, less relevant to the question of whether the Assembly was timely informed regarding 2008 revenues. In December, the financial picture for 2008 was more certain and much less favorable.

CFO Weddleton took steps to address the problem. Her December 9, 2008 emails to Mayor Begich are one of those steps. He chose not to follow her recommendations on a hiring freeze or discretionary spending, or any other steps to reduce expenditures to match 2008 revenues, (with one exception) "cosmetically" adjusting PERS, which we discuss below. Her recommendations appeared to have the support of OMB Director Phillips, but this was not sufficient for Mayor Begich to implement a hiring freeze or cessation of discretionary spending.[27] CFO Weddleton acknowledges this situation:

> Q: But it doesn't appear that it [your December 9 advice] was followed.
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> A: That's correct. You're right, but I didn't have that ability to, you know, yeah, I mean I don't know what to say to that.[28]

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[24] Id.

[25] More information and transcript excerpts are below at section entitled: October 17, 2008 work session: State of the Economy (and how it affects the MOA).

[26] Weddleton to Begich email, December 9, 2008.

[27] Phillips to Weddleton email, December 9, 2008. "This looks good. It would be great if we could get this." Weddleton had separately copied Phillips on her emails to Begich.

[28] Weddleton October 16 interview, page 16.

We asked Mayor Begich about this, and received the following answer:

> **2. What did you do in response to CFO Weddleton's email of December 9 that contained the budget risk factor spreadsheet?**
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> **a. Did you speak to Weddleton about the risk factors on or after December 9 and if so, when and what did you say?**
>
> **b. Did you discuss the risk factors with any other MOA officials on or after December 9 and if so, with whom and when?**
>
> All the "risk factors" Sharon listed in her Dec. 9 email were already well known to me and the Assembly. In fact, as we prepared to transition to the next mayor, I asked Sharon and other department heads for the full range of issues and challenges the city might face over the next several years. Most of the "risk factors" Sharon identified never came to pass or turned out for the better. Here are three quick examples: The summary indicated the city could be liable for $7 million if it lost an AWWU lawsuit -- in fact, the suit's outcome saved taxpayers millions. The summary indicated the city could be liable for $20 million in a police and first (sic – fire) medical trust lawsuit - in fact, the plaintiffs dropped the lawsuit, saving taxpayers millions. The summary indicated that state revenue sharing may be suspended due to low oil prices -- in fact, Anchorage received an increase in revenue sharing, which we devoted largely to property tax relief. In response to Sharon's email, I continued to monitor issues that could have an impact on the budget.
>
> It's worth noting that Sharon's spreadsheet did not include positive financial news about the city- I only requested a summary of potential problems. For example, the spreadsheet does not include the significantly positive financial news about the state coastal impact funds, which had not been budgeted for and ultimately totaled well over $1 million. Also at this time, we knew our liability for the PERS obligation had been eliminated and that our net assets would be boosted by more than $20 million. With this information, this spreadsheet would look entirely different.

While it is fortunate that some of the risks did not come to pass, it is equally true that some did – with the consequence of a $17 million shortfall. Mayor Begich may have closely monitored the situation, but the real issue is whether and when he disclosed the revenue shortfall to the Assembly. Since Mayor Begich did not answer parts a. and b. of our question, we do not know who from his administration he involved in monitoring the range of issues and challenges the city might face. We discuss further the missed opportunities to advise the Assembly regarding the revenue shortfall during our discussion of the revenue shortfall for 2009.

D. Did Mayor Begich know, to a reasonable certainty, that revenues would be less than appropriations for the fiscal year 2009?

1. When did he know?

We start with the understanding that until the Assembly adopts the budget and thereby makes the appropriations, it would be near impossible to know with certainty whether revenues will be less than those appropriations. [29] But recall that the 2009 budget was already approved back in 2007, as part of the biennial budget approval process, subject to a 2008 review and Assembly appropriation.[30] It is also true that available revenues change over the course of the year, especially when 1st quarter budget revisions and setting of the mill rates is taken into consideration. Nevertheless, the Charter provision is unsympathetic to these challenges. Despite Mayor Begich's assertion that a "reasonable certainty" is not achievable until after the fiscal year[31], the Charter requires an "early warning."

We know Mayor Begich knew at least by early December, given CFO Weddleton's emails of December 9. For example, CFO Weddleton's spreadsheet attached to the emails states "2008 TANS losses <u>will require cuts in Q1 2009</u>" and "Fire overspend in 2008 was funded with fund balance. <u>Will require spending reductions in 2009</u>." (emphasis added)

However, we think it is important to review more of the 2009 budget history for a better understanding of this email. We do so in the context of determining whether Mayor Begich timely reported the shortfall to the Assembly.

2. Did Mayor Begich timely report it to the Assembly?

On September 26, 2008, CFO Weddleton sent an email to Mayor Begich, OMB Director Phillips, ECD Executive Director Michael, Chief of Staff Ramseur, and Municipal Attorney Reeves. She attaches a financial markets memorandum and notes "it was my intent to keep this to one page but the issues affect everything at this point."[32] She suggests sending the attachment as an AIM to the Assembly at its next meeting.[33]

In the attachment, she provides an overview of Municipal investments and concludes with a section on 2009 issues. One addresses ML&P Commercial Paper. The other is on 2009 budget and earnings, in which she says:

> We are re-evaluating our remaining 2008 and 2009 earnings forecasts. They may be revised downward due to the interest rate and market circumstances that currently exist. Additionally, a TANs transaction would not provide any earnings

[29] This is a different issue from presenting a budget to the Assembly that has a reasonable projection of revenues supporting requested appropriations. Obviously, a budget could be introduced that, if adopted, would on its face be short on revenues.
[30] AR 2007-133 (S-1) as amended.
[31] 11-14-2009 Q and A with Begich.
[32] Weddleton to Begich, Phillips, Abbott, Michael, Ramseur, Reeves email, September 26, 2008.
[33] Id.

> in today's market so if this situation does not change the 2009 forecast will need to remove these net earnings.
>
> The Municipality will closely watch this issue. On one hand, if the markets continue to struggle in 2008 there is a large likelihood that during 2009 the unrealized losses will "amortize to par" as investments mature or reverse into a higher market value. In more simple terms, the struggles of 2008 could result in a positive year in 2009 and therefore a budget adjustment at this time is not considered necessary. But by Quarter 1 budget adjustments, the status of 2009 will become evident and the budget may indeed require an adjustment.[34]

There was no AIM from the Begich Administration to the Assembly on this topic until October 28, 2009.

On September 29, 2008, on the eve of introduction of the 2009 budget, in response to email questions from Assembly member Starr regarding whether the Municipality's cash position was adequate to handle day to day needs, Weddleton answered:

> **Yes, we are OK cash wise.** You are correct about the $100m in Tax Anticipation Notes (TANs) that were sold to carry the MOA until property tax proceeds were received. The TANs transaction has historically been a profitable deal for the MOA (sell debt at 1.92%, earn 3% or 4% tax free). However, if we were to sell TANs today it would be unprofitable (sell debt at 7%, earn 2%). So in 2009 we would only sell TANs if: a) the market returned to normalcy or b) we had no choice and truly needed the cash. **Fortunately, the MOA has two accounts that hold "sticky cash" (about $200m). The TANs were on top of the sticky cash. What this means is that instead of issuing TANs in 2009, we could liquidate our sticky cash if we had to.**
>
> We are working on a summary of all of these issues. There are other trouble areas including bond insurance, the MOA trust fund, etc**. But I would say that due to a mixture of prudent financial management and some fortunate timing the MOA is actually looking relatively secure both on the debt side and on the investing side.**[35]

a. Mayor Begich October 1, 2008 Press release

On October 1, Mayor Begich issued a press release which stated, in part, the following:

> Begich met with top city managers Monday to review the city's fiscal position. They delivered following status report to him:

[34] Id.
[35] Weddleton to Starr email, September 29, 2008.

Fund balances healthy - City fund balances are healthy because of a requirement imposed in 2002 to maintain an 8.25 percent fund balance, which Begich increased in 2004 by 2.5 percent. This enhances the city's standings in financial markets and ensures adequate rainy day savings during periods of economic turmoil.

Investments protected – In 2007, the city implemented new investment practices with the creation of a Municipal Cash Pool, which invests public funds in three portfolios of different durations. By investing the bulk of funds in the most liquid portfolio, the Municipality has retained liquidity and also minimized investment losses.

* * * * * * * * *

"Anchorage is more fortunate than most because we have adequate liquidity to endure market turmoil in the coming months," Weddleton said. "Our focus on liquidity and diversification has reduced the impacts to our portfolio. The city has avoided complex investments such as structured investment vehicles that have hurt other governments."

As he submitted the Fiscal 2009 budget to the Assembly Tuesday, Begich said Anchorage will continue to closely examine the impacts the current turmoil could have on city operations in the coming year.[36]

b. October 10, 2008 work session on the 2009 general government operating budget

At the October 10, 2008 work session on the 2009 general government operating budget, the Begich Administration gave its initial, high level overview of the 2009 budget, utilizing a Microsoft Powerpoint presentation. One of the first slides was entitled "Municipality's Financial Position Relative to Other Governments" and contained the following bullets:

Investment portfolio is liquid
Accounting practices have been updated to post unrealized gains and losses timely
Prudent bond sales
Bond underwriter changes
Strong fund balance reserve policies
Conclusion: budget does not require an amendment at this time (emphasis added)[37]

We transcribed the October 10 work session and incorporate significant portions of it here for purposes of showing exactly what was disclosed at that meeting.[38] We have put into bold items that need particular emphasis for later discussion in this report.

[36] Anchorage Well-Positioned to Weather National Economic Crisis, October 1, 2008.
[37] Slide 19.
[38] Matching the transcript with the PowerPoint presentation gives the reader an exact understanding of the subject matter being discussed.

During the initial, high-level overview, the Begich Administration offered the following:

> **Weddleton:** So today what we would like to do is do two main things; do a high level review to see where we were in '08 and where we are today, talk about the PERS a little bit, talk about revenues and expenses, take a look at the tax cap and then take a look at anything that is particularly new to 2009 that wasn't in the original '09 budget, such as new positions or requests from the departments that we are asking for your support on.[39]
>
> * * * * * * * * *
>
> **Weddleton:** The Administration is proposing 16 million dollars in anticipated (indiscernible - interference with recording) tax relief (indiscernible - interference with recording) have to last two years, 13 new police officers will be brought online, the new Park Ranger Safety Program that Elvi discussed, funding for the Eagle River Library moved to Valley (indiscernible - mumbling) Centers and then finally, the voter approved O&M costs.
>
> Here is where we can go from the 2009 approved – that the Assembly approved last year down to what we are asking for support from this year or alternatively, we can look at the 2008 revised. So we could take 2008 and bring us down to 2009, **and you will see that salary and benefit costs are anticipated to go up by 11 million dollars, but they are offset by changes in PERS** that we will discuss in detail as well as small other things that we will talk about, the Convention Center, which is simply a pass through and then finally, additional requests (sic).[40]
>
> * * * * * * * * *
>
> **Weddleton:** So here is our tax requirement. What this does is it shows expenditures and revenues from 2009 approved – so this is a year old, to the 2009 proposal in front of you now, and what it shows is that we are proposing spending to the cap, but that our total expenditures are going down mostly due to PERS.[41]

After presentation of the various pie charts on changes in PERS accounting, and revenue and expenditures, the Assembly engaged CFO Weddleton in a short discussion of real property valuations. After Weddleton indicated the slide did not include commercial property, Assembly member Drummond stated:

> **Drummond:** And the elephant in the room is what is actually going to happen, you know, with the markets in turmoil right now. I am concerned that is the beginning of a very hard to predict slide in one direction or another.

[39] October 10, 2008 work session, pages 6-7.
[40] Id., page 7.
[41] Id., page 10.

WEDDLETON: So far, Anchorage has been very fortunate, but it does remain to be seen whether or not our luck will hold out.

Drummond: Thank you.[42]

In context, this is a reference to the effect the financial markets might have on real property valuations in Anchorage. It does not appear to be intended to reflect directly on the 2009 budget. However, it is part of a more general theme that is present in all of the information generated by the Begich Administration and shared with the Assembly. That theme seems to be one of guarded optimism and no current budgetary changes are needed. This theme is carried through in the remainder of the initial overview provided by the Begich Administration:

WEDDLETON: So one of the things that I think we have sort of addressed is what is happening today? We are in untried times right now and how do we set a budget when we don't know what is going to the value of our homes, when we don't know what is going to happen to interest rates and when we don't know what will happen to the cost of any debt we issue?

So we thought we needed to address it today and we will also address it at the capital budget work session because, of course, capital budget is heavily reliant on the cost of debt. **The Municipality has very much in the last 30 days scrubbed and scrubbed and rescrubbed its situation so that we can speak about it today and unlike a lot of other governments, we are very fortunate that our investment portfolio is very liquid and this can become important if in the upcoming year we have trouble issuing debt. If we have trouble issuing debt, we have flexibility that other governments don't have and you all will be hearing from me this afternoon about this topic.**

Number two, our accounting practices have become more conservative this year. **What we used to do was (indiscernible - interference with recording) interest income, realized gains and losses and amortization during the year and then at the end of the year, like a snapshot from a camera, we reported any unrealized activity and normally that was the right way to do it because normally you had an unrealized gain and you didn't want the departments to spend that money, but our situation this year is fundamentally different.**

So we have changed the way we look at midyear unrealized activity and we are now reporting unrealized losses during the year so that all of the departments know what their real earnings are.

Additionally, we have been very, very fortunate historically with our bond sales. Most governments have a mixture of fixed rate debt and variable rate debt, let's say 75%/25%.

[42] Id., page 15.

> **We have lost a couple of underwriters and they have been replaced. <u>We had implemented strong fund balance reserve policies and I think that will help us weather this storm and finally, our conclusion at this time is that the budget doesn't require an amendment.</u>[43]**

We note the opportunity to specifically discuss the projected losses in revenue passed without mention. Additionally, the opportunity to mention the higher risk-taking in investments had led the Begich Administration to the decision to change its accounting practices regarding unrealized losses also passed without mention. There was focus on the cost of future debt, which became the theme of the October 17 work session, but nothing up to this point in the meeting discussed actual revenue loss projections known to the Begich Administration.

Near the end of the presentation, the discussion turned to the slide entitled "Challenges."[44] The slide has three items listed: Interest Revenues, MUSA, and Fund Balance. At this slide, CFO Weddleton had the following to say:

> **Weddleton: Our challenges are -- we have talked about the economy. We have talked about the elephant in the room and then, additionally, fund balance.** Now why would fund balance be a challenge? I think we put another slide next that talks about the fund balance. Yeah (affirmative), there we go. The fund balance policy requires that the Municipality not spend every penny it gets, but instead save in two ways.

Notwithstanding its prominence in the "Challenges" slide, there was <u>no</u> presentation by Weddleton on interest revenues up to that point in the work session; she had only talked about how the portfolio was "liquid" and about the new policy of tracking unrealized losses. They did not talk about "interest revenues." There was not a discussion of how much in interest revenues the city had lost to date or predicted to be lost by year's end. Thus, this was another missed opportunity to advise the Assembly that lost revenues were a quantified challenge. Instead, the Assembly was led directly into a discussion of fund balance.

c. Fund Balance

The fund balance policy in effect required 8.25% of the prior year's revenue from all general funds to be maintained. It also required an additional 2% to 3% of the prior year's revenues for the 5 major funds.[45] Amounts over the reserve are potentially available for appropriation and may in fact be appropriated over the course of the budget year.

During her initial introduction of the presentation, CFO Weddleton stated "We had implemented strong fund balance reserve policies and I think that will help us weather this storm."[46] Later, when this agenda item was reached under the "Challenges" slide, she explained fund balance

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[43] Id., pages 16-17. (emphasis added)
[44] Slide 30.
[45] AR 2004-154.
[46] October 10, 2008 work session transcript, page 17.

was a challenge because as revenues increase, so does the amount needed for fund balance, given the calculation used to determine the amount needed (i.e. 8.25% of the prior year's revenue, etc.).[47] She describes the process as occurring during first quarter of the next year, when revenues for the prior year are conclusively known:

> **WEDDLETON:** The 2007 year has been closed and the fund balance as of 12-31-07 has been balanced, but we don't know yet how much fund balance we will have to find and set aside for the calendar year 2008 **because the revenues**, **although they are budgeted and we can make pretty good predictions, aren't known until the year is closed.**
>
> **ASSEMBLYWOMAN SELKREGG:** So it is at the end of the year that we actually calculate it?
>
> **WEDDLETON:** After year -- after the end of the year, that is right.
>
> **ASSEMBLYWOMAN SELKREGG:** Okay, and so because it is uncertain, you -- we, in fact, might find ourselves pushing up against the tax cap and therefore, having to go back and find reductions elsewhere. Is that how you understood (indiscernible - speaking simultaneously)?
>
> **UNIDENTIFIED SPEAKER:** That's correct.[48]

At this very moment, the Begich Administration could have disclosed to the Assembly that Treasury's forecast of revenues is the "pretty good prediction" of a revenue shortfall of $4.9 million for 2008 that Weddleton alludes to. And, the Begich Administration could also have recapped that the Assembly had up to that point appropriated $7,028,773 of the fund balance remaining from 2007.[49] As of the end of September, 2008 the fund balance had been tapped over the course of 2008 by additional appropriations and it was known that an additional $1.7 million due to Fire Department expenditures was looming.[50] Ultimately, $9,009,391 in fund balance was used over the original 2008 budget.[51]

The shortfall in 2008 revenues, coupled with the depletion of fund balance, is of significant importance to the Assembly in its deliberations on the budget. As of the October 10, 2008 work session, simple math would have demonstrated the unreserved fund balance from 2007 had already been reduced approximately $7 million through Assembly appropriations and could very likely go down another $5 million due to the revenue losses projected by Treasury in the absence of budget reductions or increases in other revenue. We understand Municipal finances are not simple and we do not mean to oversimplify the calculations involved. But, there is a difference between calculating the reserve requirement for the next year (which was the focus of the Begich Administration's presentation) and advising the Assembly of the current fund balance.

[47] Id., page 27.
[48] Id., page 32.
[49] 2008 Fund Balance Appropriations, prepared by OMB November, 2009.
[50] At the December 12, 2008 Assembly work session, the AFD Chief acknowledges the shortfall was known in August of 2008.
[51] 10 year fund balance report, July 2009.

Weddleton's presentation focused on the difficulty in budgeting for the fund balance reserve requirement for the next year because it is predicated on the prior year's revenues, which are not known until near the end of the 1st quarter of the following year – which is obviously 4-5 months after the budget is approved. The Assembly understood the problem:

> **ABBOTT, MUNICIPAL MANAGER:** And the uncertainty that we don't know the answer to now is how we are going to end 2008, which is why we don't spend a lot of time trying to figure out the fund balance until the first quarter.
>
> **WEDDLETON:** Once a year.
>
> **UNIDENTIFIED SPEAKER:** Which is why it is on the risk sheet rather than the opportunity sheet that, you know, that you were talking about before because if revenues don't come in as we expect or for whatever (indiscernible - speaking simultaneously).....
>
> **ASSEMBLYMAN STARR:** Yeah (affirmative), I understand that. Let me ask another question though, if I can?
>
> **UNIDENTIFIED SPEAKER:** No, absolutely.
>
> **ASSEMBLYMAN STARR: Which relates to the question I put to you guys yesterday, which was when are we going to see the proposed fund balance adjustments? Are we going to talk about that today or.....**
>
> **WEDDLETON:** No, that will have.....
>
> **ASSEMBLYMAN STARR:** The answer was that we were going to get some information about projected fund balance adjustments or needs to adjust balances on an email I sent yesterday (indiscernible - speaking simultaneously).....
>
> **WEDDLETON:** (Indiscernible - speaking simultaneously)?
>
> **ASSEMBLYMAN STARR:** I think it was from Wanda.
>
> **PHILLIPS, OMB DIRECTOR:** I think I was referring to quarterly reports that we will be getting at the end of the month.
>
> **UNIDENTIFIED SPEAKER:** Okay.
>
> **ASSEMBLYMAN STARR:** That's true.
>
> **UNIDENTIFIED SPEAKER:** It will be the departmental budget to actual (indiscernible - speaking simultaneously).....

ASSEMBLYMAN STARR: But we already know that we have to adjust the fund balances right now from the numbers you are seeing even though we don't know the complete number until 2008 so do.....

ABBOTT: And that much is budgeted.

UNIDENTIFIED SPEAKER: Okay.[52]

ASSEMBLYMAN STARR: I guess that is where I would like to go with the discussion because we already know that we have to adjust some fund balances and can we see that or when will we see sort of the summary of fund balance adjustment needs as they are.....

ASSEMBLYMAN STARR: Yeah (affirmative), today or a forecast, I mean, you guys are.....

WEDDLETON: The report that Wanda was describing is more of a, you know, year-to-date spend versus -- and year-to-date revenue. It is not going to give you a perfect picture of what you are seeking.

ASSEMBLYMAN STARR: And I am not asking for the exact dollars, but we had a significant fund balance adjustment to the Police Department requirement last year which sort of [was] another reason why we went to the quarterlies was we could sort of see it transpire.

WEDDLETON: Yes, right, right.

ASSEMBLYMAN STARR: So what isn't part of the quarterlies is the fund balance adjustment required.

WEDDLETON: That is right.

ASSEMBLYMAN STARR: So what I am asking for is in the course of the next month or so, can we see the fund balance adjustment to date necessary, as well as what you guys forecast through '08?

WEDDLETON: You will see valuable information that can show you what the picture looks like, but it is not going to be exactly what you want.

ASSEMBLYMAN STARR: But to increase the fund balances, we have to increase the mil rate?

UNIDENTIFIED SPEAKER: Or decrease the.....

UNIDENTIFIED SPEAKER: The mil rate is going to be driven off the tax cap.

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[52] Transcription notations regarding indiscernible text are omitted for ease of reading.

ASSEMBLYMAN STARR: I understand that.

PHILLIPS: And that is set separately. **So if we are up against a tax cap (indiscernible - too far from microphone) we are up against the tax cap and we realize we need to shore up our fund balance by a million dollars. Let's say we close the year. We are short a million. It automatically, sort of by default comes out of savings, the fund balance.**

ASSEMBLYMAN STARR: Yeah (affirmative).

PHILLIPS: That means in part of our balancing act in the first quarter, we are going to have to find that million. You are already at the cap. We are not going to be able to tax (indiscernible - too far from microphone) could. You were right. I think that the code would allow us to do it, but I think historically we have not done that. **We have sought to balance it, which would mean reductions or savings from somewhere (indiscernible - interference with recording). Does that make sense?**

UNIDENTIFIED SPEAKER: Remember the.....

ASSEMBLYMAN STARR: It does, except I remember the discussions at the first quarter budget review when, in fact, we should see some actual fund balance needs today, for example. You know that you have to adjust the fund balances in some capacities. Sometimes it is a shuffling of the dollars from one fund to another.....

UNIDENTIFIED SPEAKER: Right.

ASSEMBLYMAN STARR: .....but the other one is the capital contribution required to pull it off. **So I would rather have that knowledge earlier than the first quarter.**

UNIDENTIFIED SPEAKER: (Indiscernible – speaking simultaneously) **we should have that quarterly report to you soon.**[53]

* * *   * * *   * * *

ASSEMBLYMAN COFFEY: No, you have got a fund balance, 20 million bucks. You know today you are two million short. Is the two million accounted for in the materials you are giving to us?

UNIDENTIFIED SPEAKER: No.

ASSEMBLYMAN COFFEY: You are just not doing anything about it?

[53] October 10, 2008 work session transcript, pages 33-37.

UNIDENTIFIED SPEAKER: That is why it is on the risk category.

UNIDENTIFIED SPEAKER: Because we don't know what we are going to need next years.

ASSEMBLYMAN COFFEY: Okay, where.....

UNIDENTIFIED SPEAKER: The 20 million is in there.

ASSEMBLYMAN COFFEY: But the quarterly report we are due to get here in October.

UNIDENTIFIED SPEAKER: (Indiscernible - too far from microphone).

ASSEMBLYMAN COFFEY: Yes, is -- will show us where we stand with those five accounts?

UNIDENTIFIED SPEAKER: Year-to-date.

UNIDENTIFIED SPEAKER: Yes.

ASSEMBLYMAN COFFEY: Year-to-date, no, I understand and it is a function of expenditures and review.[54]

* * *   * * *   * * *

ASSEMBLYWOMAN SELKREGG: It is a follow-up on Mr. Coffey's question. So if we have a sense, we could have a general sense of this figure, why haven't we included it in our budget (indiscernible - too far from microphone)? I mean not – and then make an adjustment in our first quarter budget because it seems to me to not -- to go into it not acknowledging at least a ballpark figure puts us in a position where we are either going to be up against the cap and have three -- I mean, I just don't understand why we wouldn't at least have a placeholder there.

UNIDENTIFIED SPEAKER: It is just -- it is a choice. I don't think the City has ever.....

ASSEMBLYWOMAN SELKREGG: Done that?

UNIDENTIFIED SPEAKER: .....you know, budgeted for an anticipated growth in fund balance during the initial budget approval process. It -- we are not necessarily adverse to it. It is going to mean some different choices, but I don't think it is better or worse than the methodology that we are using.

[54] Id., page 38.

> **ASSEMBLYWOMAN SELKREGG: So it is going to mean different choices now or it is going to mean different choices in the first quarter budget review.**
>
> **ABBOTT: Well, we just don't know what the answer is going to be at the first quarter. I mean, there literally are, you know, let's assume that we are 400 million dollars roughly, just a scale of the five major (indiscernible - too far from microphone). Let's assume that we are three quarters the way through the year and the expenses and the revenues all come in exactly on three quarters, you know, they come in at (indiscernible - too far from microphone). So we -- by now we have spent 300 million and we have collected 300 million. <u>So let's say over the last quarter, we are, you know, something changes five percent. That is five million dollars. So if you are -- the challenge would be then -- we don't know if that five million dollars is going to be there by the end of the year when we finally settle it out, but we might be there after nine months. So should we then try to fix a five-million-dollar problem or shall we wait until March and April when we know exactly what it is and then deal with it? That is the challenge. We -- you could get some wild swings in money. These are small percentages, but big dollars.</u>**
>
> **ASSEMBLYWOMAN SELKREGG: But are big in (indiscernible - speaking simultaneously). Yeah (affirmative), which makes me, as a conservative, think well, shouldn't we be having a little pile in the original budget that addresses it, but I am just asking the question. I am not proposing an (indiscernible - speaking simultaneously).[55]**

Again, the Begich Administration passed on the opportunity to disclose that, in fact, the Administration had already predicted a $5 million loss in revenues. Instead, Municipal Manager Mike Abbott states it as a "what if" scenario. The Begich Administration then leaves it to the Assembly to decide if there should be budgetary adjustments during the budget process in the Fall, over making adjustments later, at first quarter 2009:

> **ASSEMBLYMAN STARR: Well, I guess the point on the policy saving that you talk about, you know, given the financial situations of today's need to have sort of the ready cash and the fall back policy, isn't it prudent to look at reestablishing that? You are short-funded now. You are not going to see an increase in revenue between now and the first quarter that is going to reduce the funding needs. So what -- I don't see that you are going to find additional fund sources that is going to offset your current need to balance the funds today. So what.....**
>
> **ABBOTT:** I don't think I understand. I -- the fund balance policy -- it is important to remember, this isn't like a cash flow management device.

[55] Id., pages 39-40.

ASSEMBLYMAN STARR: No, no, but it is very fundamental to our fiscal health though, Mike, and that is my point.

ABBOTT: It is, but it is only measured on an annual basis. It is -- our fund balance swings wildly during the course of the year and our rating agencies and the other for whom we have established this understand that.

ASSEMBLYMAN STARR: I (indiscernible – speaking simultaneously).....

ABBOTT: We could get into a very cash deficient situation (indiscernible - speaking simultaneously).....

ASSEMBLYMAN STARR: I don't want to turn it into a debate. My point is that we have the data that we aren't acknowledging through a budget adjustment and then we have what appears to be budget creep (ph) after the first quarter adjustment requirement when, in fact, we could do something to the budget now that would put everybody on notice.

ABBOTT: And I am not disagreeing with you.

ASSEMBLYMAN STARR: Okay.

ABBOTT: That if you guys could set, you know, we are going decide that we have, you know, we want to prevent a big adjustment at first quarter so we are going to fill a five million-dollar hole right now or a two-million or three or (indiscernible - speaking simultaneously).....

ASSEMBLYMAN STARR: I agree and that is why I am after the quarterly through the third quarter because you are going to see Fire Department probably and, you know, these other ones that blind sided us, if you want to use that term, the last time we had to adjust those budgets and they were a surprise when they shouldn't -- they don't need to be is what I am getting at and it.....

ABBOTT: It is a policy choice.....

ASSEMBLYMAN STARR: I know.

ABBOTT: .....that is certainly available to the Assembly.....

ASSEMBLYMAN STARR: Okay.

ABBOTT: .....to deal with that now rather than at first quarter.[56]

During the next week the Begich Administration provided a document to the Assembly that addressed questions from the work session, including questions on fund balance.[57]

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[56] Id., pages 41-43.
[57] GGOB 2009 Proposed-Updated Request for Information from: 10-10-08 work session.

In reviewing the document prior to distribution to the Assembly, CFO Weddleton noted there was a shuffling between funds to meet the reserve fund balance policy.[58] They discuss how the funds are "robbed" and Weddleton asks what happens if, despite this shuffling, there is still a shortage.[59] OMB Director Phillips ends with:

> We balance to it in 1st quarter. So in essence we fund it with the next years taxes; or in other words we under spend in the next year to fund it. It looks and feels just like a 1.3m request that we have to fund. Mike Abbott was kind of right when he said we cut budgets to fund it. <u>We have never actually cut spending to fund it but in truth we under spend what we could to fund it. Maybe the best way to say it is that at 1st qtr. we plan to generate a surplus in the coming year to shore up the shortfall. We plan this by treating it just like a required expenditure we have to fund.</u> If you look at the reconciling sheet for the ordinance you will see that the shortfall is treated like an expenditure rolling onto the property taxes.[60]

The document indicated fund balance for the five major funds as of the end of 2007 was $26,945,354 and at the end of the 1st qtr of 2008 was short $1,385,718 from meeting the reserves policy, assuming the emergency reserve target was 2.1% (we note this is at the low end of the 2% - 3% target range).[61] This information failed to include any expenditures of fund balance since the end of the 1st quarter 2008. Since these expenditures were through publicly available Assembly Resolutions, the information could have been included.

As to fund balance <u>projections</u>, the response to the Assembly was "This is being prepared. It requires coordination between several departments."[62] The report was provided to the Assembly on November 17, 2008. Given the context in which it was requested, including the work session exchanges transcribed above, it is our opinion the fund balance report provided to the Assembly on November 17 was misleading. Primarily, it was misleading because it used revenues and expenditures based on the last 12 months (October 2007 to September 2008), instead of the fiscal year data (January 1, 2008 through September 30, 2008) and a 2008 year-end projection based on the same fiscal year data. This had the effect of projecting year end unreserved fund balance for 2008 at $34.5 million, when in fact fund balance was heading for a final number of $17.5 million.[63] More problematic, the November 13, 2008 spreadsheet gives the impression there is $8.8 million available to spend <u>after</u> the bond reserves policy is met, when in fact we now know the fund balance ended up short of meeting the bond reserves policy by $9.3 million.[64] Given the fund balance reserve policy is set based on prior year revenues, the use of a trailing 12

[58] Weddleton to Phillips email, October 16, 2008.
[59] Weddleton to Phillips email, October 17, 2008.
[60] Phillips to Weddleton email, October 17, 2008.
[61] Id., page 2.
[62] GGOB 2009 Proposed-Updated Request for Information from: 10-10-08 work session, page 2.
[63] Comparison of fund balances from 11-13-08 worksheet provided to Assembly on 11-17-2008 and fund balance data provided to Assembly at work session on 11-13-2009. See AIM 105-2009(A).
[64] Id.

months will not, and in fact did not, accurately reflect to what degree fund balance was in or out of compliance with the reserve policy.[65]

d. October 14, 2008 Assembly Meeting

Our review of the meeting minutes did not disclose any discussion amongst Assembly members or with the Begich Administration regarding the state of municipal finances or the 2008 or 2009 budgets. The first public hearings were held on the 2009 budgets. The Local 302 CBA was approved at this meeting.[66]

The Mayor did provide the Assembly a written report entitled "Upcoming substantive issues" dated October 14, 2008. Two issues in that document spoke to finances of the city:

> <u>City fiscal condition</u> – The administration recently performed an analysis of the impacts that the current national financial crisis is having upon the Municipality. If found that overall; Anchorage is better positioned than most U.S. Cities to deal with this crisis. The two main areas of concern are; 1) investments (how are the Municipality's investments performing, are these investments still considered liquid, and should the 2009 budget be adjusted in some way?), and 2) debt (is the Municipality able to issue new debt, does our current debt portfolio expose the Municipality to increase interest costs, and will we have to liquidate any assets in order to manage our debt portfolio?) <u>The results of the analysis are generally positive, although the Port's Commercial Paper program is an area that may require temporary lending from the MOA until the financial markets return to normalcy.</u> (emphasis added)
>
> <u>Fiscal 2009 city budget</u> – the administration submitted to the Assembly on Sept. 30 a Fiscal 2009 city budget that is nearly $5 million less than approved last year while continuing the city's investment in new police officers. The "continuation" budget constitutes the smallest budget increase in at least six years and maintains the city investments in relieving traffic congestion, promoting a positive business climate and protecting public safety. The most significant new initiative is the addition of 13 more police officers, continuing the administration and Assembly's effort to add a total of 93 new police officers to the force over the past six years. <u>The overall budget proposal is only about $4 million more than last year, just about a 1 percent increase.</u> Three public hearings on the operating budget are scheduled for Oct. 14, 28 and Nov. 18. Final action by the Assembly is expected on Nov. 25. (emphasis added)

e. October 17, 2008 Work Session: State of the Economy (and how it affects the MOA)

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[65] AR 2004-154 requires an unreserved general fund balance in an amount equal to 8.25% of prior year revenues and an unreserved fund balance in the five major funds in an amount equal to 2.5% of prior year revenues.
[66] AR 2008-186.

It has been asserted the Assembly was fully informed regarding the Municipality's finances at an October 17, 2008 work session. Mayor Begich and CFO Weddleton[67] have made the assertion, as did Acting Mayor Claman at an Assembly meeting in January, 2009. We cannot find support for the assertion in the available records. There was a 2 hour budget work session scheduled for that day. However, it was cancelled. In its place was a 1 hour session related to the national economy and its affect on municipal borrowing. Weddleton provided a Powerpoint presentation at the bond work session.[68] The presentation includes a general discussion of the difficulty in selling bonds in the market. Her presentation as to how the Begich Administration viewed the Municipality's situation is summarized in one of her first slides:

> MOA is in a good position
>
> Low per capita debt
> No variable rate debt (whew!)
> Primarily 20 year debt (not 30 year)
> Strong investment liquidity (short duration)
> Strong bond rating
> Low "real" investment losses[69]

The presentation goes on to show examples of what selling bonds in the market might look like and what effect the market may have on the Port of Anchorage's Commercial Paper. The presentation also covers the ability of the Municipality to sell Tax Anticipation Notes in 2009. In this part of the presentation, Weddleton asserts the Municipality will not likely be able to use TANs and therefore "will cover cash flows with cash on hand."[70] This may have been a vague reference to using fund balance. It was a missed opportunity to discuss the projected revenue losses already known to the Municipality.

The next slide states "Investments are Sound (Sep 29)", and displays a table that shows unrealized losses of $12 million and "real" losses of $2 million ($10 million and $1.6 million of which are MOA), which we reproduce here:

	Construction Pools				Operating Pools				Total			
	AC	MV	URL	"Real"	AC	MV	URL	"Real"	AC	MV	URL	"Real"
MOA	$210	209	1	-	373	364	9	1.6	583	573	10	1.6
ASD	46	46	-	-	95	93	2	0.4	141	139	2	0.4
Total	256	255	1	-	468	457	11	2	724	712	**12**	**2**

AC = Amortized Cost MV = Market Value URL = Unrealized Loss "Real" = unrealized loss that is likely to be realized.

While her own Treasury staff are predicting a revenue shortfall on the 2008 budget of $4.9 million as of the end of July (reported September 23, 2008), Weddleton made a presentation to the Assembly showing only $1.6 million in real losses. Here is what she said at the beginning of the meeting, before showing the above table:

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[67] Begich to Wheeler letter, November 10, 2009; Weddleton to Coffey email, January 20, 2009.
[68] State of the Economy (and how it affects the MOA).
[69] Id., slide 17.
[70] Id., slide 29.

> **WEDDLETON: But, one of the important things is to talk about these losses. <u>Have we actually lost any money? Well, not really</u> because what has happened is they might have an advertised cost of let's say, close to par, a million dollars, and right now if we sold it, we might only get $900,000. So, we have an unrealized loss of $100,000. But, in the underlying investment -- let's say it's a Fannie Mae or a Freddie Mac -- if the underlying investment is sound, the investment should pay out in part when it matures. So, the vast majority of our losses right now are unrealized losses, and we'll actually show you some numbers later in the presentation.[71]**

Later in the meeting, she said the following:

> **WEDDLETON: <u>The Municipality is in an extremely good position compared to most other governments</u>. We have low per capita debt. We have absolutely no variable rate debt, unlike most governments. We have almost exclusively 20 year debt instead of 30 year debt. So, think of how you feel if you have a 20 year mortgage instead of a 30 year mortgage. You would feel a lot more financially secure, all of the things being equal. <u>We have strong investment liquidity because our investments have a short duration. We have a strong bond rating. And, as we talked about before, the difference between an unrealized loss and what we think will actually come to fruition, we have very few real investment losses that we think we will actually experience.</u>[72]**

Turning to the above table, this is the entirety of what is said about the table:

> **WEDDLETON: Now, let's talk about investments. Sheila [Selkregg] had mentioned investments. Our investment strategy has been conservative, and so we've been fairly fortunate. What this does -- here is the Municipality's investment portfolio as of September 29th, and it shows you what we have in the construction cash pool. And, remember that we're required by the bond agreements to invest construction bond proceeds in the most conservative investments almost humanly possible. So, we anticipate absolutely no losses in our construction cash pools that we are using for our capital programs. And, out of $210 million, our unrealized losses are actually -- I don't want to use the term only, but they are only $1.0 million. So, for a pool that size in today's in market, that's actually fabulous. Now, our operating pools are not legally restricted. So, we do have a figure here which shows you that our current strategy at September 29th had an unrealized loss of $9.0 million dollars. <u>However, that's comprised of U.S. government backed investment securities that we feel reasonably confident will mature in part and we won't incur a loss. However, we do believe that we will incur some losses because we have</u>**

[71] October 17, 2008, Assembly work session excerpt, page 2.
[72] Id., page 3

> **<u>some exposure to Lehman Brothers, Lawmou (ph), et cetera. But, overall, here's our total figure. We have almost $600 million, and we believe that this [referring to the $1.6 million "real" MOA losses], at the end of the day, will be our realized losses.</u> If we had avoided risk at all over the last year and a half, we would have lost $10 million of investment income. So, I would encourage the Assembly to continue allowing us to continue with this because it's a sound investment strategy, and these numbers really prove it. Very few investment portfolios of this size can claim that, but now let's talk about the trust fund.**[73]

Again, we believe the presentation is a missed opportunity to share with the Assembly the information prepared by Treasury. CFO Weddleton's prediction of losses of only $1.6 million were not put into context in terms of the impact on the 2008 or 2009 budgets. Nor is the number $1.6 million easy to reconcile with Treasury's analysis. Treasury indicated in its Analysis there were 4 offsetting decreases in revenue. One was $1.1 million in interest revenue ($524k for TANs, $114k for Construction Pool, and $416k for Cash Pool Short Term Interest).[74] Another was $1.4 million in unrealized gains removed from the Cash Pool Short Term Interest earnings projection.[75] There are differences in the purposes and methods used to create the Treasury data and the presentation data. We are not suggesting they should exactly match, but we do make the point that much more information on revenues was available at this time, but not shared with the Assembly. The Begich Administration's "Real" number presented to the Assembly may be accurate insofar as it goes. But, it is not the full picture. Treasury was including all revenue sources for its analysis of the 2008 budget. The October 17 presentation to the Assembly only addressed investments in the Cash Pool. This presentation therefore cannot support the contention that the Assembly was fully informed at this work session.

f. Mayor Begich October 23rd press release

On October 23, Mayor Begich issued a press release which stated, in part, the following:

> "Across America, cities are being forced to lay off thousands of employees and deeply cut back services to weather the national economic crisis," Begich said. **"Fortunately, Anchorage's finances are sound and we expect city services will continue to be delivered without interruption, if the crisis is dealt with by the federal government relatively soon."**
>
> Cities across the country are taking dramatic steps to deal with the economic crisis.
>
> **"Anchorage is more fortunate than most because we have adequate liquidity to endure market turmoil in the coming months," said municipal Chief Fiscal Officer Sharon Weddleton. "Our focus on liquidity and diversification has reduced the impacts to our portfolio. The city has**

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[73] Id., pages 4-5.
[74] Analysis of General Government Revenues as of July 31, 2008 (presented September 23, 2008).
[75] Id.

avoided complex investments such as structured investment vehicles that have hurt other governments." [76]

While the general theme expressed in this release and his release of October 1, that Anchorage is in better shape than most other cities is true, its combination with the budget presentation which recommends no changes, the lack of information regarding the projected investment losses, and revenue shortfall, and the fund balance situation, led to understandable consternation in January of 2009 when the Assembly is advised for the first time of a $17 million budget shortfall for 2009.

g. October 28, 2008 AIM to the Assembly on the Municipal Investment Portfolio

The Begich Administration presented the annual report to the Assembly on the Investment Portfolio at the Assembly's October 28, 2008 meeting.[77] In it, the Begich Administration indicates that "From June 2007 through August 2008, the MOA aggregate portfolio earned a return of 4.13%, trailing behind the composite benchmark by 38 basis points."[78] The report also states that the concept of starting the Cash Pool in 2007 remains "sound" and has enhanced earnings over the past strategy by $7.8 million.[79] The report continues on to say that as of August 31, 2008, the portfolios complied with investment guidelines.[80] It also notes that current market conditions may "persist into 2009" and the "bottom may be yet to come."[81]

While all of this is presumably true, there is nothing in the report that discloses the investment revenue shortfall contained in Treasury's "Analysis of General Government Revenues as of 7/31/08 (presented September 23, 2008)", or any new data on losses between the end of July and mid-October.

h. November 14, 2008 Assembly work session on the 2009 budget.

We reviewed a transcript of the November 14, 2008 work session.[82] The first portion of the session covered budget issues regarding Solid Waste Services (SWS).[83] The Assembly then received information from CFO Weddleton on how vacancy factor is calculated and included in budgeting.[84]

After this, the Assembly moved into a discussion with the Begich Administration about fund balance.

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[76] Business Week, Wall Street Journal Give Anchorage Top Rankings, October 23, 2008.
[77] AIM 86-2008.
[78] Id.
[79] Id.
[80] Id.
[81] Id.
[82] November 14, 2008 work session.
[83] While not covered in this work session, there is an issue with regard to how PERS journal entries particularly affected SWS, which are addressed elsewhere in this report.
[84] Id., starting on page 43.

PHILLIPS: The fund balance I have been slated on your information to have that to you today. Accounting has -- Sharon and I just received it from accounting. They're researching one small anomaly so we should have that to you shortly. It's likely going to be a range because it's such a wide estimate at this point, but it will give you at least a feel.[85]

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ABBOTT: .....under accepted revenue, and that's why the fund balance -- we understand your question, and it's valid. You are more likely to see variation, much more likely to see variation on the revenue side than you are on the spend side.

STARR: And, that's where I want to look, Mike, because this is where our budgetary realization needs to come from.

ABBOTT: I agree.

STARR: Because, are we setting realistic budgets based on revenue trends? And, if we already know we're doing a big adjustment and we're short sighting our revenue again, then I don't want.....

ABBOTT: That's what we're trying to give you the information that you've asked.

STARR: So, to say it's never been used before for a budgetary discussion.....

ABBOTT: Not in November.

STARR: <u>I understand, but the point is we just shouldn't be adjusting budgets for first quarter if we kind of know about it now.</u>

ABBOTT: <u>And, that's -- and to the extent that there is good data that we give you, you are going to get it. But, we have not generated that for this kind of a discussion in November in -- since any of us have been here.</u>

STARR: And, I get it. A revenue trend by a budget would do it, too. And, right now, we're seeing expense tracking but we've never done -- I've never requested a quarterly (indiscernible - simultaneous speaking).

ABBOTT: And, the challenge on revenues – you know, on most of our revenue Accounts, I think we could give you down to within the $10,000 increment. It's very good, and Sharon's group has made dramatic improvement over the last five years.

[85] Id., page 62.

STARR: Perfect.

ABBOTT: **The challenge is going to be interest income. <u>Would anybody here like to tell us what year-end interest income will be on the Municipal investments</u>?**

WEDDLETON: Especially when you include unrealized gains and losses. It's not the interest income that's the challenge.

ABBOTT: It's the loss.

WEDDLETON: It's the market, Marked-to-market.

STARR: Well, the study will have the revenue forecast to date sort of in it and that's.....

ABBOTT: It'll have -- and that's why you'll probably get a range, Bill. That's why you'll probably get a range of -- because we still have a lot of information yet to glean, some on revenues, some on costs, and that's why I would predict that you are going to get a range. And, I wouldn't even speculate without looking at it what the sort of the range in billions [sic] of dollars would be.

STARR: It shows a lot of the health of the City based on the fund balance currently. And, then, it shows the obligation based on our revenues for the next budget year. That's what I think it does.

ABBOTT: Good. Okay. .. follow up on that quickly.[86]

The remainder of the meeting was largely on the police revenues, possible Assembly budget amendments, and a discussion on holding a police academy for new police positions. Again, the opportunity was there to advise the Assembly about the ongoing revenue projections prepared by Treasury for year-end 2008, as it affects fund balance.

i. November 13/14, 2008 emails between Begich and Weddleton

Weddleton emailed Mayor Begich regarding Assembly-requested budget amendments.[87] In order to pay for the amendments, CFO Weddleton recommends the Mayor offer to slightly delay the hire of new police officers. She goes on to justify the recommendation:

Why?

1. We can't mess with vacancy factor anymore. We're already stretching it, and Elvi has publicly stated that any more changes to vacancy factor are a shell

[86] Id., pages 63-66.
[87] Weddleton to Begich email, November 13, 2008.

game and that we'll be back in front of the Assembly when everyone blows their vacancy factors.

2. We can't cut IT (Sheila's earlier recommendation) because IT will likely be expected to absorb CSA with only one new FTE in 2009. This effectively represents a cut to IT.
3. We can't cut Finance/CFO (Sheila's earlier recommendation) because that lapse is what pays CSA's loan at the end of each year. The loan won't disappear even if CSA disappears.
4. We can't cut FTEs because if we did so, we would need a corresponding reduction to vacancy factor (i.e. a wash).

The big elephant in the room is investment income. Right now we have about $10m in unrealized losses which probably won't reverse by 12/31/08. So adhering to our fund balance policy will be a huge problem this year. Most likely, 1st quarter budget revision will be painful. (emphasis added)

My strong recommendation is to respond with a single voice as any more amendments come through – the source of funding is to delay the hire dates of the new Police Officers. This is a legitimate cut (vs. a fictional cut) that helps the Assembly understand the tradeoffs of adding new items elsewhere.[88]

Mayor Begich responded:

Re you ok with the s version that we have prepared to close the budget? I would like to have a memo from you once the budget is complete to let me know the risk factors we have on elements of the budget.
Thanks.
You guys did a great job.[89]

We can only conclude from the above exchange that Mayor Begich was now aware, even prior to final adoption of the 2009 budget, that the revenues would not support the appropriations planned in the budget. We believe his request here for the Risk Factors is the genesis for CFO Weddleton's December 9 emails.

j. Analysis of General Government Revenues as of September 30, 2008 (Presented November 18, 2008)

On November 18, 2008, Treasury released to Mayor Begich's Executive Committee its latest report comparing budgeted revenues for 2008 to the year-end forecast. The forecast was a $5 million shortfall, of which $1.2 million was due to a change in Federal Reserve lending rates in October. The report also noted Fund 181 (Building Safety) was also under by $2.8 million.

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[88] Id.
[89] Begich to Weddleton email, November 14, 2008.

k. November 25, 2008 Assembly meeting

Mayor Begich distributed the Budget Advisory Commission's assessment of the 2009 budget at the November 25, 2008 Assembly meeting, without comment. The one-page assessment does not note any revenue shortcomings. According to the minutes, when the BAC assessment came up before the Assembly, Assembly Member Birch noted these were extraordinary economic times with declining oil prices and a potential shortfall of state revenue sharing. He also stated that because of the national economy, there were concerns about locking into five-year labor contracts.[90]

Later in the meeting, the Assembly began deliberations on the 2009 budgets.[91] There is no indication from the Begich Administration of any issues with the ability of revenues to cover the 2009 budget. Some of the Assembly members spoke to the uncertainties of the world and national economies, but none gave any indication they were aware of the true nature and extent of municipal revenues. Mayor Begich spoke to the budget. He did not mention any shortfalls regarding revenues, difficulty adhering to the fund balance policy, or the CFO's prediction that 2009 first quarter budget revisions would be "painful."

l. December 16/17, 2008 Assembly Meeting

On December 16, 2008, the APDEA and IAFF contracts were before the Assembly for their adoption. Prior to the meeting, Assembly member Starr sent emails to CFO Weddleton and OMB Director Phillips regarding the state of municipal finances. The exchange was as follows:

> **Starr:** On going financial uncertainty in major indicative aspects of our economy such as stock market indicies and investment portfolio's continues to present itself with negative growth and threats of deflation. This means key investment accounts, cash accounts, and interest earnings accounts will provide less return.
>
> Alaska tourism revenues are forecast to be lower as some forecasters (Cruise Ship Industry) state that year to date bookings are down 40% over last year this time. I would assume this trend continues to rental car and hotel motel in Anchorage.
>
> State oil revenues have fallen drastically with low prices. This potentially could have an impact on the disbursement of State revenue sharing to communities.
>
> **Given these baseline statements, your experience, and up to date fiscal indicators you monitor, can you estimate their effects on Anchorage finances near first quarter close?**
>
> **Can/will you officially certify that given the approved 2009 budget, recent increased spending (AMEA, IBEW), and proposed increased spending**

[90] November 25, 2008, Assembly Meeting.
[91] We did not transcribe the lengthy portions of the budget discussions. The audio recording is publicly available.

(AFD, APD, CSA, and other cost overruns), that anticipated 2009 revenues of the MOA will exceed forecast 2009 expenses per your professional opinion?

Weddleton: This is not something I can easily address in e-mail. Perhaps it's a conversation that should happen at either the Assembly level or be forwarded to the Budget and Finance Committee for evaluation. I am not trying to be non-responsive, however, I am uncomfortable making an assertion like this within an e-mail.[92]

Starr refined the question in an email 5 minutes later:

Starr: Can/will you officially certify, as of today, that anticipated 2009 revenues of the MOA will exceed forecast 2009 expenses per your professional opinion?[93]

There is no known email response from CFO Weddleton, but records do indicate she forwarded Starr's emails to someone. We have been unable to determine who the email was forwarded to.

At the December 16, 2008 Assembly Meeting, Mayor Begich gave his last report as Mayor.[94] He did not mention the status of Municipal revenues.

When the Assembly took up AR 2008-333, which would require monthly financial reporting, including on the financial status of revenues, Assembly member Selkregg spoke to the resolution, but gave no indication she was aware of the current dire situation with respect to municipal revenues. She only mentioned certain municipal funds were tied to world and national financial markets.

Mayor Begich supported postponing the resolution, stating "we just saw these tonight." He said he thought it would be important for both the OMB Director and CFO to review the resolution. He did not disclose (and may not have known) CFO Weddleton had actually worked on the resolution and it's AM.[95] Instead, he focused on media reports on how Anchorage was in a better position than other cities. Nor did CFO Weddleton advise the Assembly she had worked on the resolution and had reviewed drafts prepared by the Assembly's counsel. Assembly member Ossiander noted the resolution was prepared with the assistance of the Finance Department. When asked about what the resolution might require, if adopted, CFO Weddleton said she could supply the revenue information. Assembly member Selkregg agreed to postponement.

AR 2008-334, regarding a hiring freeze, was then also postponed, with minimal discussion.

CFO Weddleton asserts in a letter to this office that, prior to this meeting, Assembly member Selkregg met with her and OMB Director Phillips, saw the risk factor spreadsheet, and agreed

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[92] Starr to Weddleton email, December 16, 2008. Weddleton to Starr email, December 16, 2008.
[93] Starr to Weddleton email, December 16, 2008
[94] This and the remainder of the statements attributed to the December 16 meeting are taken from the recordings.
[95] We asked Begich when he first knew that CFO Weddleton was working with Assembly members on the two ARs. He said he did not recall. 11-14-2009 Q and A with Begich.

with Weddleton's recommendation regarding a hiring freeze, and CFO Weddleton agreed to help Selkregg "because of my belief that this was an important topic that needed to be debated by the Assembly."[96] Selkregg acknowledges meeting with CFO Weddleton before the 16th meeting.[97] Selkregg states CFO Weddleton "seemed concerned about financial issues, but did not provide details."[98] Selkregg states she had not seen either the December 9 email from CFO Weddleton to Begich or the spreadsheet.[99]

When the Assembly turned to approval of the APDEA contract, there was debate amongst Assembly members about the ability of the Municipality to afford the contract. Yet, the Begich Administration did not take the opportunity to advise the Assembly about how bad the revenue picture was. The Assembly only spoke in general terms, in regard to the world and national economies - there is no indication they were aware they were on the brink of a $17 million shortfall.

In response to Assembly questioning, Chief Heun said APD would absorb the $388,000 overage presented by the APDEA contract within its approved 2009 budget. CFO Weddleton has asserted she advised the Assembly of $3.5 million in annual cost overruns related to the contracts.[100] Weddleton has also asserted that she thought her communication "would cause the Assembly to reject these two contracts."[101] The two emails to the Assembly on the APDEA and IAFF CBAs both indicated a possible increase in costs for 2010 related to performance pay – which if fully utilized could climb costs to over $3 million, but both also state: "OMB reviewed this proposed contract specifically in relation to the 2009 Updated Operating Budget. The new items negotiated in the contract are materially covered in the 2009 Operating Budget. OMB estimates that [$388,000 for APD and $330,000 for AFD] in costs are not included in the 2009 budget. [APD and AFD] will be directed to absorb this cost differential during 2009."[102] If CFO Weddleton thought the contracts were too costly and should not be approved, she did not say so publicly. We understand this. It can often be the case that senior officials privately disagree with a policy decision of the Mayor's. In any event, the Mayor speaks for himself and he supported the contracts.

The next day, the Assembly took up the IAFF contract. Assembly member Starr followed up on his earlier email questions about the state of municipal finances by asking questions of CFO Weddleton. The relevant exchange is as follows (with emphasis added):[103]

> **STARR:** I have two questions. Are you seeing a tightening of our ability to meet our expenses? Do we have the cash flow? Do you feel comfortable in our current financial position? The second question is; as we increase these expenses, we need to find places where revenues will increase. We are increasing costs across the board for these labor contracts. **So the question is; are you comfortable**

[96] Weddleton to Wheeler letter, November 12, 2009.
[97] Selkregg to Wheeler email, November 9, 2009.
[98] Id.
[99] Id.
[100] Weddleton to Wheeler letter, November 4, 2009.
[101] Id.
[102] Weddleton to Assembly members email, December 15, 2009.
[103] December 17, 2009 Assembly meeting transcript, pages 1-6.

with where we are at? The second one is; where do you see the revenue coming from to pay for the bills in that?

WEDDLETON: Through the Chair, Mr. Starr, we are in unprecedented times. However, this Municipality is more fortunate than most. The reason for that is because our property taxes are budget driven and not mil rate driven. So most communities as assessed values go down, have steep declines in property tax revenues.

Most communities right now are having steep declines in sales tax revenues and most communities are having steep declines in income tax revenues. That does not mean that we are immune to what is going on in the world today, but one of the items you mentioned was State revenue sharing and my understanding of the Governor's budget which was announced earlier this week is that she has committed that the State revenue sharing will be at least what it was last year, which is exactly what we budgeted.

So if you look at the pie and look at the amount of revenues in 2009 that are comprised of property taxes and State revenue sharing, those are our safe revenue sources. Unlike most communities, that makes up the bulk of our revenues. So compared to most communities, we are more fortunate.

ASSEMBLYMAN STARR: Again, the question; when we increase expenses, where does the revenue come from, and I guess you didn't also indicate to me where your comfort level was with the revenue accounts and some of the other revenue sources that we get from investment incomes. Are we seeing a retraction in our investment pool monies available?

WEDDLETON: **There are <u>two</u> issues when it comes to investments. One of the issues is the MOA Trust Fund and the MOA Trust Fund is invested quite similar to the Permanent Fund Corporation.** The MOA Trust Fund supplies a dividend which in 2009 has been budgeted at seven million dollars. Because it is invested similar to the Permanent Fund, the MOA Trust Fund has incurred a market decline.

However, my recommendation to the Investment Advisory Commission when it met earlier this week was that we should not panic, but rather I would like to propose to this Body a code amendment to make sure that the corpus of the trust fund is protected and the code amendment would be something like this; effective January 1, 2010, the maximum dividend would, instead of being up to five percent of the prior, I think it is 20 quarters' market value, be a maximum of four percent of the prior 20 quarters until the corpus of the fund has been replenished and that would allow us to do two things. It would allow 2009 to not incur a decline in the dividend, but it would allow us to very slowly and carefully and cautiously regain the corpus of the trust over of about a 10-year period of time.

> The Investment Advisory Commission and I discussed that earlier this week and I do think that if we can craft some language and it would be short, maybe one or two sentences that they would be supportive of that language and we would bring it to you as an Assembly when they meet and they meet on a quarterly basis.
>
> **ASSEMBLYMAN STARR:** And again, the replacement for the lost revenues that we are likely to see in other aspects then, you know, it is obvious that the State and then the property taxes are where we are going to see the replacement of that lost revenue (sic). Is that sort of where we get it? I mean, that is kind of obvious to me. Is [are] there other revenue sources that we can tap into, State grants, Federal grants? What else do we have coming in?
>
> **WEDDLETON:** This Municipality is extraordinarily aggressive in pursuing all grant revenues it has available to it and we have been very, very successful in doing so. We don't intend to suddenly stop pursuing grant revenues and we do try to seek additional grant revenues when they are available.

CFO Weddleton never addressed the elephant in the room. She did say there were two issues with respect to investments, but only covered one – the MOA Trust Fund. The elephant – investment returns and revenue generally, was not mentioned. She could have informed the Assembly her own staff had just produced its analysis showing $7.9 million in projected total general government revenue shortfall compared to 2008 budgeted revenues, excluding fund 181.[104] Adding in Fund 181, Building Safety, resulted in a total shortfall of $11.2 million.[105] The cost of the labor contracts, according to CFO Weddleton email below, adds another $6 million. There is no indication the Assembly was aware of these aggregate numbers.

The 2009 shortfall is often blamed on investment returns, but there is more than just those returns. The CBAs, according to a Weddleton email to Coffey on January 20, 2009, are also part of the problem: "So of the $17m problem, slightly less than $6m represents the contracts."[106] In the same email, she says that $10 million in unrealized losses was disclosed at the October 17 work session:

> **Coffey's question:** When did the City know that the investment performance would result in a shortfall?
>
> **Weddleton:** The first troublesome month was September, the results of which were quantified on about 10/15. October results (quantified on about 11/15) and November results (12/15) increased the scope of the gap. Recall that at the Assembly work session held on October 17, the following topics were discussed:
>
> a. How the economy affects the MOA's ability to issue GO debt and commercial paper

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[104] Analysis of General Government Revenues as of 10/31/2008 (presented December 17, 2008).

[105] As of December 30, 2008, the projected various, excluding Building Safety, grew to $9 million. Larson to Weddleton, Abbott, Phillips, Ellis, Allen, Moore, Mullane, Reeves, Raiskums email, December 30, 2008.

[106] Weddleton to Coffey email, January 20, 2009.

b. How the economy may preclude a TANs sale in 2009 (and the impact that would have upon earnings)

c. An evaluation of the cash pool earnings, which noted a $10m unrealized loss for general government at that time

d. A discussion of the MOA Trust fund and its MV decline, including the size of the annual dividend paid from the trust fund.

We have also discussed this topic quite a bit at Assembly meetings.[107]

As noted earlier in this report, the portrayal in October was that the $10 million was not a concern. And, as we have noted previously in this report, the revenue shortfall projections were being produced by CFO Weddleton's staff as early as July of 2008 and were projecting "realized" losses for the 2008 budget at that time.

Coffey's question: When did the City know that the investment performance was in the range of $9M?

Weddleton: See answer to 4c. The 10/17 worksession communicated an estimate of $10m. Note that one change between that earlier presentation and the presentation on 1/13 was that there was still a possibility in 2008 that the markets could recover. By 1/13/09, chances of a 2008 recovery had passed. Additionally, November 2008 had some investment transactions that incurred realized (vs. unrealized) losses. **<u>Though the impact to the budget was the same, because we started marking to market during 2008, the realized losses effectively precluded the chance for recovery in late 2008 or 2009, since they were no longer merely paper losses</u>. (emphasis added)**

One point - the investment figures in the 1/13 worksession were estimates. As of 1/13/09, December 2008 investment performance had not yet been calculated and recorded on the books. Additionally, until the 2008 books are truly closed (around 3/31) they are subject to many adjustments.[108]

CFO Weddleton states above that the losses were known as far back as September and discussed with the Assembly on October 17, 2008. The implication, of course, is the Assembly knew the situation back in the Fall of 2008 and nevertheless took no action, or worse – chose to increase spending. However, a review of what was presented to the Assembly shows that while some of the information was shared with them, not everything was disclosed and what was disclosed was greatly minimized by the administration, including the specific recommendation that no action with respect to the budget was necessary.

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[107] Id.
[108] Id.

m. Executive pay raises.

In response to the suggestion that the Begich Administration was, in fact, very concerned about municipal finances as of December 17, 2008, we juxtapose the following. During the December 17 Assembly meeting, Municipal Manager Abbott sent an email to Chief of Staff Ramseur, CFO Weddleton, Municipal Attorney Reeves, and ECD Executive Director Mary Jane Michael:

> I spoke with Mark this evening. I suggested we implement a 3% across the board salary adjustment for all the execs that have been in their jobs for most of 08. We might want to convene to discuss any special cases (I have one or two).
>
> Mark is willing to take this action right now to make sure we get it done before we are in acting-mayor mode.
>
> Your thoughts?[109]

CFO Weddleton responded:

> My recommendation would be to include the utilities, enterprise funds and authorities in this change. ML&P is in a transition and this would help them get through their first year. I am reluctant to allow the utilities a larger (say, 6% raise) because I do believe we need to hold on to all execs we can and flight to the utilities is a risk as they are perceived to be safer.
>
> The utility boards could still take action to do more than 3% but if we move forward and implement a raise they would have to explain why their execs were allowed a double dip.
>
> We should <u>exclude</u> all Assembly/Ombudsman, and internal audit staff.
>
> I agree that time is of the essence.
>
> I think we should each limit ourselves to a maximum of two special cases (two for Mike, two for Jim, two for Mary Jane, and two for me). We had an excessive number of special cases last year and the overall adjustment was affected.[110]

In response to an example from Municipal Attorney Reeves, CFO Weddleton responds:

> Actually, my recommendation was an average of 3% for each of our departments, except that we can each pull two employees out of the calc and handle them separately.

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[109] Abbott to Senior Staff email string, December 17, 2008 sent between 6:45 and 7:06 p.m.
[110] Id.

Example:
Bob 1%
George 1%
Tom 2%
Sue 2%
Sam 3%
George 3%
Average for all but two of the employees 3%

Two special employees carved out for separate consideration.[111]

On December 31, ECD Executive Director Michael asked Municipal Manager Abbott, "When do we need to have this done by?" Abbott responded, "Friday. It needs to get done by Mark."[112] The raises were not carried through until January 2, Mayor Begich's last day.

We want to be clear here that we do not mean to suggest that the pay raises were not well-deserved; most probably were. And, it has been the historical practice that municipal executive employees and non-represented employees receive wage increases similar to their union co-workers. What is of concern is the timing and the circumstances.

n. One last opportunity.

The Anchorage Daily News (ADN) had been seeking investment and other financial information from CFO Weddleton during the latter half of December. On December 22, 2008, she finished reviewing or drafting a memorandum that she may have intended to share with the ADN. First, however, she sent the memorandum to Mayor Begich.[113] And then she sent it to the Assembly.[114] Notwithstanding that Mayor Begich had imputed knowledge that the revenue shortfall for 2008 was projected to be $7.9 million for the 5 major general government funds and another $3.3 million for the Building Safety fund, the memorandum to the Assembly does not mention this. Instead, it says that "Overall, the Municipality's management of its cash pools has been reasonably successful" and "Over the last 3 months, the total municipal cash pool has experienced a negative return of 1.45%. However, the negative return is substantially driven by unrealized losses rather than realized losses. Because the underlying investments are substantially sound, we believe that the unrealized losses can recover over time."[115] The memorandum also includes a header that says "2009". Underneath, it says, "Inevitably, 2008 investment activities will affect 2009. As the year draws to a close, we will continue to communicate the Municipality's financial condition to you, the Assembly, to ensure as much transparency as we can in our financial circumstances."[116]

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[111] Id.
[112] Id.
[113] Weddleton to Begich, Abbott, Reeves email, December 22, 2008
[114] Weddleton to Assembly email, December 22, 2008.
[115] Id.
[116] Id.

E. The Notable Exception – "Cosmetic" adjustment of the 2008 budget

Although Mayor Begich did not take all of CFO Weddleton's suggestions, there is one notable exception. It appears that Mayor Begich did endorse, or may have endorsed, CFO Weddleton's idea to "cosmetically" adjust department budgets through a reversal regarding PERS.

The treatment of PERS "on behalf" payments by the State was a hot issue in 2008 amongst those involved in government accounting. A simplified description of "on behalf" payments is that they are the State's contribution to local governments' obligation to PERS. Effective July 1, 2008, the State capped local governments' obligation at 22%. The State pays the difference between the 22% paid by the Municipality and the actuarially determined amount. In 2008, this "on behalf" difference was approximately 15%.

The hot issue amongst local governments was whether and how to reflect the State's "on behalf" payments in the local governments' books. This issue is also a "red herring" for purposes of this report. The "red herring" is how the PERS payments were journaled and reported for purposes of Comprehensive Annual Financial Report (CAFR). [117] It is our understanding that PERS was appropriately journaled and reported in the CAFR, in accordance with the recommendations of the Municipality's independent auditor and in accordance with GASB.

The real issue is how the budget for the PERS payments was treated in 2008. It is our understanding from our review of emails on this issue and in interviews with staff that the PERS activity was not adjusted in the 2008 budget to reflect the way it was finally journaled and presented in the financial reports. The significant effect of this omission is that the difference between the amount the department actually spent compared to the amount budgeted was more than it would have been if the budget had been adjusted downward to reflect the way PERS was finally presented in the financial statements. For example, by not adjusting the budget downward the Police Department came in under budget by $13,000 for the year. But if the budget had been adjusted downward to reflect the way PERS was eventually presented in the financial statements, the Police Department would have been over budget by $600,000 for the year. This was known, because the same issue was discussed amongst OMB and Finance regarding the first half year entries:

> Teresa, has the journal entry to post the additional PERS expense (the difference between our pay in and the actuarial amount that we receive PERS relief for) been posted? This is critical as it was budgeted and I need it to post otherwise all of the departments will look like they have budget capacity.[118]

Departments benefitting from this change would have included the Police Department, which in the past had significant revenue shortfalls and other budgetary issues that were a matter of

[117] AMC 6.40.030.
[118] Phillips to Peterson, Weddleton, Fritz email, July 11, 2008. See, also Peterson to Phillips, Weddleton, Ellis email, August 4, 2008.

concern for the Assembly.[119] But, it also would have included Fire, Law, and Transit: "We need the 6 months PERS journal entry reversed for Legal, Transit, Fire, and APD. We need this ASAP."[120]

In addition, to the extent that departments could now appear able to spend more, there was no revenue to support this difference. The potential for "overspending" this presents is evident in the emails. The Begich Administration was aware of this problem; it explains why the reversal of the last ½ year PERS journal entry was done late in the year (December 15, 2008):

> **Phillips:** The problem is that several departments are sitting in (sic) invoices waiting for this budget authority. We could also just do budget over-rides but that will trigger a lot of work for the Controller's division.
>
> **Weddleton:** I am not that concerned with sitting on invoices. The departments should have managed their budgets in 2008. They were told to not "spend" the PERS entry. So let's meet halfway. Could we reverse on **12/15** (to partially minimize year-end spending) and issue a memo **now** telling departments to cease optional purchases?[121]

The Assistant Controller explained her concern about doing individual department changes, and the possibility of spending fund balance without assembly appropriation. In response, Weddleton replied:

> Your points are valid and sound. This is a tough situation. **I am nervous about 1st quarter (due to what you're mentioning below but also what has happened to our yields in the cash pools).**
>
> I would say there is no discipline for Departments to manage their budgets because there are simply no consequences for over-spenders. Wanda and I would like to change this, and we have about a dozen ideas that could change this dynamic on a go-forward basis.
>
> I recall back when I was Controller – that was the year when we had lost $20m in state revenue sharing and every department (well, most every department :)) had taken deep cuts. That year, even with deep cuts, every single department met its budget.

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[119] For example, this exchange between Assembly member Coffey and Municipal Manager Abbott at the November 14, 2008 work session: COFFEY: Are the cops estimating revenue accurately this year? Are you done with that craziness? ABBOTT: They will be – I don't know if they are going to be at 100%, but they will be within 95% of their -- now, let me back up. There is the revenues that -- the 151 Fund, which is the police fund, gets -- the vast majority of its revenue from property taxes, the mill rate associated with that. That's it.

[120] OMB Director Phillips email to Controller, December 4, 2008. Based on our review of the data, we think Transit may actually be a reference to Traffic.

[121] Weddleton to Phillips email, December 4, 2008. (emphasis added)

> On the 16th the MOA will be asking for a supplemental appropriation for one serious over-spender. It will be interesting to see how the Assembly will react to this request.[122]

Later that day, OMB Director Phillips emailed CFO Weddleton and the Controller:

> Sharon
>
> I had a follow up conversation with [the Controller] regarding today's issue with the reversing the JE for PERS based upon your decision to not book PERS affective [sic] July 1, 2008. **Whether to book this JE or not had nothing to do with budget but was a policy decision you have made. The timing of this JE both originally and the reversal have a significant budget impact, hence my involvement.** [The Controller] explained to me that [the Assistant Controller] refused to book the JE as she believes strongly she has a responsibility to not allow departments to exceed their budget as she has to account for fund balance at the end of the year. This is at least the 4th time this year [the Assistant Controller] has blocked actions solely because of her concerns on budget not accounting. It appears she truly believes she is personally responsible for the budget and ultimate fund balance compliance. I do appreciate your desire to cultivate a questioning environment and I appreciate that having dedicated staff is a good thing. However, [the Assistant Controller] is creating a difficult in [sic] environment for my staff to get their jobs done in. I reviewed the Code because I thought maybe I was the one confused about the Controller's role regarding the budget. This is the only section I found. It does not appear to support [the Assistant Controller]'s position. [The Controller] and I have tried to work the issue with [the Assistant Controller] many times this year and we have been unsuccessful. There has to be some middle ground that supports a solid internal control environment but does not take days of my staff's time to convince [the Assistant Controller] of our position. The only one OMB should have to "convince" is you. After that it should be a matter of communicating. That is not how it has been. Can you help us?[123]

A day later, OMB Director Phillips urged:

> Regardless of the accounting outcome I still advocate that this should not be budgeted. Just got to plug for my area :) I am on the board so I will do my best to push this issue.[124]

An alternative to this plan would have been to go to the Assembly to modify the 2008 budget. This appears to have been under internal discussion - at least up through November of 2008, as noted in an email from the Assistant Controller to Candace Beery at SWS: "So in order to have budget loaded for these transactions please coordinate with [OMB] to have it included as part of

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[122] Weddleton to Ellis, Phillips, Peterson email, December 4, 2008. (emphasis added)
[123] Phillips to Weddleton, Peterson email, December 4, 2008.
[124] Phillips to Peterson, Weddleton, Gibson email, December 5, 2008.

her Supplemental Load for PERS Fiscal Relief Adjustment as an impact to SB 125 …that she is bring to the Assembly."[125]

As far back as July of 2008, CFO Weddleton stated:

> They (sic) Mayor has decided to do a budget amendment for PERS for all of the MOA (including utilities). Dr. SOA revenue, CR. PERS expense. 7/1 through 12/31. Impact: you will no longer have to book an entry for Qu3 and Qu 4 (but will still have to book Qus1 and 2).

As early as October 17, 2008 OMB Director Phillips stated:

> We will be moving the PERS reduction forward shortly. I would like to fold all of the 'housekeeping' items into it so there is one action that re-aligns the budget as necessary for year end. The one exception to this is Fire. It is so large it would be hard to fold in; however we could if that is the preference.[126]

On October 22, 2008 CFO Weddleton said the following:

> Re: the PERS AIM, I agree that one might be able to claim it was covered in the work session. But it's a stretch. I wonder if when we submit the docs for the 2008 budget amendments if we could expand on PERS then. Particularly if we're going to transfer 7/1/08 to 12/31/08 PERS expenditure authority from underspending departments to overspending departments as our source of funding. <u>I agree with your point when we were with Mike [Abbott?] (that the revenues have dried up, too) but I think it might help get Assembly support, particularly if they don't think too hard about it.</u>
>
> <u>If we don't use transferred PERS expenditure authority I can't imagine what else we could do.</u>
>
> <u>As an FYI, we might also try and use the 2008 PERS expenditure authority as a source of funding to pay off the CSA loan. If we could make the CSA loan disappear then our CSA options go way up and 2009 looks far better.</u>[127] (emphasis added)

OMB Director Phillips replied:

> That is a really good idea on CSA. I am on point with most of the AIMs so I don't' think this should worry you. The only one in your court is PERS but why don't you let me prime on that and send you something. We can either put it in an AIM or with the budget documents. It will be easier for you to change a document

[125] Beery to Weddleton email, November 21, 2008.
[126] Id. Email string in OMB folder.
[127] Weddleton to Phillips email, October 22, 2008.

> than right a whole new one. I envision it will be something like History, Changes, Impact, etc.[128]

In discussing how to address Law's shortfall, Municipal Manager Abbott was still anticipating going to the Assembly as lat as November 6, 2008.

> Ok. We'll wrap this budget amendment into the muni-wide version for introduction on Dec 2 and action on Dec 16. The contract change can be intro'd and passed on Dec 16.[129]

We at this point do not know why the "housekeeping" was not taken to the Assembly. We do know that the Fire Department problem and a taxi cab litigation settlement were funded out of fund balance in December, 2008, as approved by the Assembly.[130] It may be that the Begich Administration did not want to face the Assembly's scrutiny or criticism, as suggested by CFO Weddleton in her email correspondence with SWS in regards to its budget problems:

> **Weddleton:** It looks like you can squeeze by. Am I wrong? Note that a supplemental appropriation is something to be avoided whenever possible. PERS is <u>not</u> a reason for a supplemental appropriation. [131]
>
> **Beery:** Administration can't squeeze by with the $92,690 PERS expense. Even without the PERS expense, administration will be short ($14,369) in personnel.[132]

The impact of the PERS treatment included significant benefits to SWS. SWS found itself potentially exceeding budget authority by over $700,000, which included the unbudgeted expense related to PERS in the amount of $243,650.[133] The conversation on the topic of SWS's budgetary issues had started as early as November 18.[134] On December 15, Weddleton notified Beery that due to the pending PERS reversal, there was also going to be "credit" for some personnel expenses.[135] We have not examined further what the final shortfall for SWS was or how it was covered.

As mentioned above, the Department of Law may have also benefited. Law's Indigent Defense Contract was underfunded in the amount of $498,000 and set to expire at the end of October, 2008. OMB and Law had known the contractual shortfall was going to happen as far back as March of 2008, but the decision to push it off into the Fall of 2008 and use supplemental appropriations instead.[136] We believe the reason the contract was under funded was because Law was exploring creating a Municipal Public Defender agency in 2007 to see if this would save

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[128] Phillips to Weddleton email, October 22, 2008.
[129] Abbott to Reeves email, November 6, 2008.
[130] AR 2008-303, approved December 16, 2008.
[131] Weddleton to Beery, Madden, Phillips email, December 2, 2008.
[132] Beery to Weddleton, Madden, Phillips email, December 2, 2008.
[133] Beery to Peterson, Ellis, Phillips email, December 10, 2008.
[134] Beery to Weddleton email, November 21, 2008.
[135] Weddleton to Peterson, Beery, Ellis, Phillips, Deegan email, December 15, 2008. This appears to be related to a State error in the amount of $631,934.98.
[136] Reeves to Phillips email, March 17, 2008.

money. The potential savings were taken into account in the budget by underfunding the contract for 2008, even though the Public Defender program was nowhere beyond exploration, let alone implementation. The idea of a Municipal Public Defender was eventually scrapped.

Law prepared an Assembly Resolution for an additional appropriation.[137] Law was trying to get the AR on the Assembly's October 14 agenda. It was stopped at the Municipal Manager's level: "I think we should hold this until we talk to the Mayor on Monday. It is essentially an admission that the MOA won't stay under budget this year."[138] The item was not put on the Assembly's agenda. Recall that on October 17, 2008 OMB Director Phillips responded, "We will be moving the PERS reduction forward shortly. I would like to fold all of the "housekeeping" items into it so there is one action that re-aligns the budget as necessary for year end. The one exception to this is Fire. It is so large it would be hard to fold in; however we could if that is the preference."[139]

Law's AR was not introduced until December 16, 2008, with no Assembly Memorandum. The public hearing was set for January 6, 2009. The AR was postponed indefinitely at the request of the Claman Administration.[140] No reason was given on the record.[141]

We asked Mayor Begich about his involvement with the PERS issue:

3. Were you involved in decisions made after Dec. 1, 2008 regarding the treatment of PERS "on behalf" payments in the 2008 budget?

> **a. Did you give direction to (sic – or) concur in giving direction to any MOA administration officials after July 1, 2008 to make journal entries regarding PERS "on behalf" payments. If so, what was the direction given?**
> **b. Did you concur with, endorse or give direction to take any MOA administration action after July 1, 2008 regarding the treatment of PERS in the 2008 MOA budget. If so, what was the direction given?**
>
> No. PERS accounting is handled by the Municipality's Controller Division. I understand that external auditors were directly involved in the ultimate decision on this issue and that we received a clean audit report for 2008.

We did not find an Assembly agenda item on this issue between November 1, 2008 and December 31, 2008. The PERS journal entries posting first ½ year and last ½ year costs were posted in August and the reversal of the last ½ year was posted December 15, 2008. The 2008 budget was not adjusted to reflect the reversal for the last ½ year journal. Thus, it is our understanding that the financial reports and CAFR were correct, but the budget in PeopleSoft was not adjusted to reflect the way PERS was finally journaled and presented.

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137 AR 2008-325.
138 Abbott to Weddleton, Phillips, Westover, Reeves email string, October 10, 2008.
139 Id.
140 January 6, 2009 Assembly Meeting.
141 Id.

On December 18, 2008, CFO Weddleton emailed Assembly Chair Claman in regards to setting up a work session on the MOA Trust Fund ordinance. In it, she says:

> 1/16 for a worksession is good. But I may need to ask for some flexibility on the time. On 1/16, there is an AGFOA conference that will have a very important topic – accounting for PERS. Though it sounds benign, the CPAs in Alaska are having a pretty heated dispute from community to community. It actually matters because if the MOA's position (that we should only record the 22% we pay to the state) does not prevail, then almost every department in the MOA will blow its 2008 spending (and 2009 will need a supplemental appropriation of many millions). So there is a lot at stake in terms of public perception ("you mean you took credit for a budget that grew by only 2% but a few months later you changed your mind?") and I would like to attend the AGFOA conference to support the MOA's position. As an FYI, this is the position that Fairbanks is taking too, which is helpful because their financials are issued before ours.[142]

A forensic audit might better develop a complete picture of how the treatment of PERS in the 2008 budget affected department expenditures, how it "cosmetically" changed the appearance of expenditure authority, and if, how, and to what extent it affected fund balance. Such an audit is not within the scope of this investigation. Nevertheless, our conclusion is that the treatment of PERS in the budget appears to be part of a larger decision to not inform the Assembly of certain 2008 budget problems, including that revenues were less than appropriations and expenditures were not what they appeared to be.

F. Remedies

Violations of the Charter can generally be remedied by injunctive relief preventing continuation of the violation, recall of officials,[143] or rescinding or voiding the action taken. The first two remedies are no longer available. . That leaves the third option, the voiding of actions taken, for consideration. The Assembly has asked that we review Mr. Levesque's conclusion that the IBEW and APDEA CBAs are void or otherwise subject to rescission, and that the IBEW CBA is otherwise subject to revision, as far as it violates public contracting policies. We have concluded that Mr. Levesque was incorrect in concluding that these CBAs are subject to rescission as being void, due to failure to comply with required precedents to approval. We further conclude that the IBEW CBA does not violate public contracting policy and law, either in its express terms, or in its application.

[142] Weddleton to Claman email, December 18, 2008
[143] Charter §3.03.

Discussion: Are there other reasons to find the CBAs invalid or voidable?

1. The Assembly's unilateral mistake does not justify rescinding or voiding these collective bargaining agreements.

As Mr. Levesque noted in his opinion letter, the Assembly cannot use its own, unilateral conduct to disavow the legitimacy of these labor agreements. This is true whether these mistakes or unilateral failures are based on lack of an adequate Summary of Economic Effects (SEE) or the CBAs were not in their final form when presented to the Assembly. It also holds true even if the Assembly was mistaken on the condition of the Municipality's finances, or any other unilateral mistake or insufficiency.

There is no evidence the unions negotiated these agreements in bad faith, or that they acted unlawfully or used fraud to induce any of the errors upon which the Assembly might consider basing a rescission effort. There also is no evidence of any mutual mistake by the parties, upon which a rescission effort might proceed. Accordingly, and as noted by Mr. Levesque, these are not grounds for rescinding these collective bargaining agreements.

Complicating the scenario by which these agreements could be unwound are two considerations. First, the focus of concern on just two contracts does not address the other contracts approved at the same time, under very similar circumstances. A legal challenge to the IBEW and APDEA contracts premised on a failure to certify funds or other code violations, or mistake of fact as to municipal finances, could not be sustained without applying the same theories to the IAFF and AMEA contracts.

Second, it is highly likely the doctrine of ratification has made defects regarding the approval process moot. "The power of a party to avoid a contract for mistake or misrepresentation is lost if, after he knows or has reason to know of the mistake or non-fraudulent misrepresentation, or knows of the fraudulent misrepresentation, he manifests to the other party his intention to affirm it or acts with respect to anything he has received in a manner inconsistent with disaffirmance, or he does not within a reasonable time manifest to the other party his intention to avoid it."[144] The table in the Background section of this report details the ratification action taken by the Assembly with respect to these contracts, including accepting wage concessions or defeating efforts to rescind by some of its members.

2. The contracts were not in their final form when presented to the Assembly.

Anchorage Municipal Code section 3.70.130A. provides "Upon completion of negotiations between the municipality and the bargaining representative, <u>all of the terms and conditions shall be reduced to writing in a single agreement.</u> The agreement shall then be presented to the appropriate employee unit for ratification and to the assembly for ratification in the same manner as a municipal ordinance." A draft of the IBEW CBA was available at the December 2, 2008

[144] Thorstenson v. ARCO Alaska, Inc. 780 P.2d 371, 374-375 (1989)(internal quotations and citations omitted).

Assembly meeting. It is 102 pages long. Nothing in the record indicates the document itself was then considered incomplete. There is no motion in the record regarding this issue. The IBEW CBA was approved on a 6-4 vote.

We are unaware of any pending allegation that the final version, as it exists today, contains any material or substantive terms different from those presented in the draft at the December 2, 2008 meeting that have not been approved by the Assembly. While it is true AR 2009-63, addressed by the Assembly on March 3, 2009, stated both that changes to work covered by the contract "were unknown and not identified during the Assembly meeting on December 2, 2009" and "Acting Mayor Claman's letter dated February 2, 2008 [sic] (Attachment 4) confirms material mistake in the contract language", AR 2009-63 was not adopted by the Assembly.[145]

Instead, the particular issues of how the CBA interacts with federal projects and whether the CBA applies to the Maintenance and Operations Department, or just the Property and Facilities Division were both resolved, as discussed below. And other issues regarding the CBAs have since been addressed by the Assembly. Thus, while certain Assembly members pointed out the possibility that the drafts presented did not contain material terms, the full Assembly has not to date concurred with that assessment and, further, any perceived defects have been cured by the subsequent actions.

We note the draft IAFF agreement was presented at the December 2 meeting under Item 9.F.11. and continued to be labeled "draft" up through the December 16, 2008 meeting and subsequently approved on December 17 on a 7-4 vote. The APDEA agreement was presented at the December 2 meeting under Item 9.f.12. and continued to be labeled "draft" at the December 16, 2009 meeting where it was approved on a 6-4 vote (Assembly member Coffey excused). The Assembly has in effect waived its right to full compliance with the Code provision.

Furthermore, we sampled some prior assembly actions on similar agreements and it may be that prior practice has long been for the Assembly to be presented with and to approve agreements, even though the agreements are not in final form. For example, the 5 year APDEA agreement approved in 1999 was presented to the Assembly as a series of Tentative Agreements, not as a single complete agreement.[146]

3. The contracts were passed with a deficient Summary of Economic Effects.

This office concurs with the Levesque opinion insomuch as the opinion notes that AMC section 2.30.050B.3. provides that a failure in compliance does not invalidate the action taken. Thus, whether the S.E.E.s were defective does not affect the validity of approval of the CBAs.

[145] Assembly members considered concurrent notices to rescind AR 2009-280, as well as AR2009-306 and AR 2009-307. With respect to AR 2009-306, the matter was withdrawn at the March 3, 2009 meeting. However, all three items were carried over to the March 24 meeting and were not then addressed, according to the Clerk's notes.
[146] See AR1999-183 and AM 649-99.

4. Fund Certification. The Levesque opinion concludes that approval of both agreements violated AMC section 6.30.050. We disagree.

This office previously advised at a recent Assembly meeting that fund certification was not required. We provide explanation here. By its own terms, the certification of funds required by AMC section 6.30.050 applies only to contracts, agreements or other obligations "involving the expenditure of money" or ordinances, resolutions or orders that are "for expenditure of money." The approval by the Assembly of CBAs neither involves nor is for the expenditure of money. Only the Assembly's subsequent approval or amendment of appropriations "involve" or is "for" the expenditure of money.

Funds certification ensures the Municipality can meet its legally binding payment commitments to third parties. A CBA is not a legally binding commitment in the same sense; it does not guarantee a payment can or will be made. It only specifies the applicable work rules and compensation package for specific job positions. It does not guarantee employment of (and thus payment to) any specific individual. Unlike contracts made with third parties, like with contractors to build a road or with professional advisors to give advice on investments, the approval of a collective bargaining agreement by itself is not a commitment to expend a defined amount of money. Should the Assembly choose to increase or decrease a department's appropriation, department employees working under the relevant CBAs may be hired or terminated in the manner specified by the CBAs, but the CBAs do not control the amount of the appropriation.

Additionally, it would be awkward at best to presume a fund certification is needed for approval of a multi-year CBA. There is no adequate way to certify funds from revenues that are not currently in the possession of the Municipality, and have yet to be collected, let alone anticipated by yearly property tax assessments and establishment of mill rates. This is in addition to the approval and sale of bonds, tax cap calculations, and many of the other fiscal activities that occur on an annual basis that either directly or indirectly affect fund balance. At worst, certification of funds for the out years of a CBA could be viewed as an invalid attempt to bind future assemblies. By Charter, budgets are proposed, adopted, and funded on an annual basis.

It must be noted the code provision at issue was part of the original Greater Anchorage Area Borough code adopted at unification over thirty years ago and remains unchanged from that time. As part of this investigation we reviewed many of the Assembly Resolutions approving or amending Collective Bargaining Agreements and the Collective Bargaining Agreements themselves that have been approved for the past 20 years. Not one has a fund certification, giving weight to our opinion that no such certification is required.[147]

5. The contracting-out requirements of the IBEW CBA do not extend to all Municipal property or all Municipal departments.

Mr. Levesque incorrectly states Section 2.14.4 of the 2008 CBA expands coverage of the IBEW contracting-out requirements. He claims this article expands coverage of the contracting-out

[147] See, List of Assembly Resolutions Ratifying Particular Collective Bargaining Agreements.

requirements only from property owned by ML&P to "all property owned, operated, maintained or constructed by or for the municipality."[148]

Article 2.14.2 of the 2005 CBA required the MOA to include as a condition of any contract or subcontract under which bargaining unit work within the jurisdiction of the Agreement was to be performed, a requirement that the contractor/subcontractor have a current CBA or letter of assent with IBEW Local Union 1547. This provision applied to more than just ML&P, as can be seen by reference to the article describing the scope of the agreement.

The scope of the 2005 CBA is described in Article 2.2 of the 2005 CBA ("Scope of Agreement"). Article 2.2 specified that, in addition to ML&P, the CBA applied to Development Services, Traffic engineering, Building Safety and Health & Human Services. Further, the contracting-out requirements applied to <u>all</u> work that could be performed by any classification for any of these named departments within the bargaining unit.[149]

When the new 2008 CBA was negotiated, Article 2.2 was modified to add Maintenance & Operations and Department of Neighborhoods to its scope and to eliminate Building Safety and Health & Human Services.[150] In all other regards, the scope of the two CBAs remained unchanged. Then, two new Articles pertaining to contracting-out were added to the CBA: Articles 2.14.3 and 2.14.4.[151]

Article 2.14.3 continues the broad application of the contracting-out language to ML&P, but no longer includes any of the other departments. The application of the contracting-out language to the other, covered, departments was moved to the new Article 2.14.4. Article 2.14.4 ended the broad application of the contracting-out language to the covered departments, other than ML&P. Instead, it limits the application of this language only to traditional electrical work, as the term is defined in that Article.[152] Rather than expanding the contracting-out requirements, as claimed by Mr. Levesque, the new CBA significantly restricts those requirements, compared to those contained in the 2005 CBA.

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[148] Levesque Opinion, September 23, 2009, p. 9.

[149] A review of the Appendix 1 to the 2005 CBA shows the bargaining unit work contained a large number of classifications, including but not limited to, mechanics, warehousemen, dispatchers, accountants, customer service specialists, clerks, engineers, student aides, paint & sign technicians, carpenters, and elevator inspectors, in addition to employees who actually handle hotwire and other electrical components of the work for these departments. Essentially, the CBA was a wall-to-wall Agreement for the listed departments.

[150] Article 2.2 ("Scope of Agreement") of the 2005 CBA reads:

> This Agreement shall apply to all facilities operated by and all operations and work conducted by Union represented employees of the MOA, *Municipal Light & Power, Development Services, Traffic Engineering, Maintenance & Operations and Department of Neighborhoods* working within classifications set forth in this Agreement.

[151] Article 2.14.3 of the 2005 CBA was renumbered as 2.14.5 in the 2008 CBA.

[152] Article 2.14.4 limits its application to departments other than ML&P and to "work within the traditional jurisdiction of the IBEW." It goes on to define that term to mean "work specifically electrical in nature. . ." and gives examples of that work.

6. The IBEW CBA contracting-out language does not violate federal law or public policy.

a. When specific federal or state funding requirements preclude the use of union signatories or letters of assent, the Municipal solicitations do not include these restrictions.

It is important to note the contracting-out requirements of the IBEW CBAs are not, and have not been, exercised in violation of federal statutes and regulations. The very letter cited by Mr. Levesque in support of his opinion[153] stands for the opposite proposition: when the Municipality determines specific federal funding rules prohibit union signatory or letter of assent requirements, those requirements are not made a condition of the particular contract solicitation.[154]

Moreover, in the case of the Goose Lake Concessions Building Upgrades project, a grievance was filed against the Municipality by the IBEW over the Municipality's decision not to require an electrical subcontractor to comply with the union signatory/letter of assent requirement of the CBA. The grievance was resolved when the Municipality agreed to comply with the express terms of the CBA.[155] In that resolution document, the IBEW acknowledged the Municipality will not require adherence to the contracting-out requirement when federal contracting law prohibits it.

b. The IBEW Collective Bargaining Agreement does not violate federal law calling for full and open competition in public contracting.

i. Reliance on President Obama's February 6, 2009 Executive Order does not support a conclusion that the 2008 CBA violates federal "full and open competition" standards.

Mr. Levesque correctly notes federal policy generally requires full and open competition in public contracting. However, he is not correct in stating, "the restriction to award contracts and, by extension, only to consider bids, by contractors who are either signatories to the collective bargaining agreement or who obtain assent from the union to perform that work, is an unallowable restriction to full and open competition."[156] He cites, without further analysis, an Executive Order, signed by President Obama on February 6, 2009, for support for his conclusion.

Examination of the Executive Order shows that, in signing it, President Obama reversed the policy of George Bush and reinstated the authority for the use of Project Labor Agreements (PLA) on major public construction projects (over $25 million).[157] Section 4 of the Executive

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[153] February 24, 2009 letter from Federal Transit Administration (Regional Administrator R.G. Krochalis) to D. Kenneth Ford.

[154] In fact, that was exactly the situation involving the cited Federal Transit Authority's letter: the contracting out language requiring union signatory/letter of assent was omitted from that particular contract.

[155] See, Grievance Resolution, 09-02.

[156] Levesque Opinion letter, September 23, 2009, p. 10.

[157] A Project Labor Agreement (PLA) is a multi-employer, multi-union, pre-hire agreement designed to systemize labor relations between multiple construction trade unions and contractors on a specific construction site.

Order requires PLAs to *"allow all contractors and subcontractors to compete for contracts and subcontracts without regard to whether they are otherwise parties to collective bargaining agreements."*

Ignoring for the moment that this Executive Order applies to PLAs and not to the kind of contracting-out provisions found in the IBEW CBA, this clause cannot support Mr. Levesque's conclusion that the 2008 CBA contracting-out requirement precludes full and open competition. Unlike the kinds of large construction projects that could justify a PLA, Municipal construction projects do not involve multiple owners or multiple union and non-union contractors.[158] Moreover, contractors and subcontractors are able to compete for Municipal contracts and subcontracts involving covered work without regard to whether they are otherwise parties to a collective bargaining agreement with the IBEW. If it is not a party to a CBA with the IBEW, and the terms of the solicitation invoke the contracting-out language of the CBA, the contractor or subcontractor can obtain a letter of assent from the IBEW and proceed with its bid on the project.

ii. The IBEW CBA complies with full and open competition in public contracting policies, in that all qualified, responsive and responsible parties are eligible to compete.

The regulations pertaining to full and open competition apply to federal contracting agencies and not the Municipality of Anchorage, and thus, are not applicable to a review of the validity of the contracting-out provisions of the IBEW CBA. To the extent federal funding sources specifically prohibit use of the contracting-out requirement of the CBA, the Municipality does not utilize it.

A review of the IBEW CBA contracting-out requirements demonstrates that it is consistent with the principles of full and open competition. All qualified contractors and subcontractors who wish to compete for Municipal construction contracts subject to this contracting-out requirement have a means for access to them. Municipal contracting procedures for these contracts use sealed bids or other competitive procedures for the solicitation, evaluation and award of these contracts, just as would be required under federal acquisition regulations, if they applied. The contracting-out requirements are not limitations on access, but merely a restriction that must be met before the bidder is qualified, much like any other allowable restriction recognized under federal contracting law. Finally, any qualified contractor or subcontractor, whether or not it is signatory to an IBEW CBA, may bid on a covered Municipal project.

The statutes and regulations calling for full and open competition in public contracting have been developed to provide for equal rights in the competition for federal contracts, subject to allowable restrictions, limitations and exclusions. While the federal full and open contracting requirements apply to federal contracting agencies, their principles are not inconsistent with the procedures utilized by the Municipality in its contracting. To better understand that, it is necessary to examine the purpose of this federal policy.

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[158] Rather than supporting Mr. Levesque's opinion that federal contracting law has become less tolerant of restrictions on public contracting, is could be argued this Executive Order actually moves in the direction of increased union influence over the coordination and prosecution of major public construction projects.

In 1984, Congress enacted the Competition in Contracting Act of 1984, Pub. L. No. 98-369 (1984), in which it adopted full and open competition as the standard in public contracting. This standard exists to provide access to public contracting to all qualified contractors who wish to compete for government contracts.[159]

Then, in 1996, Congress passed the Federal Acquisition Reform Act of 1996 (FARA), Pub. L. No. 104-106, 110 Stat. 679 (1996). In FARA, Congress chose to retain the full and open standard in public contracting and stated, "The Federal Acquisition Regulation shall insure that the requirement to obtain full and open competition is implemented in a manner that is consistent with the need to efficiently fulfill the Government's requirements."[160] In FARA's legislative history, Congress specified that this "provision makes no change to the requirement for full and open competition or to the definition of full and open competition."[161]

Federal Acquisition Regulations (FAR) governing federal "full and open competition" requirements are contained in 48 C.F.R. Part 6. The scope of FAR demonstrates that full and open competition is not a sacrosanct requirement, but is a policy that can be modified by the exclusion of sources, and other means that limit competition for federal contracts:

> **6.000 Scope of part.**
> This part prescribes policies and procedures to promote full and open competition in the acquisition process and to provide for full and open competition, full and open competition after exclusion of sources, other than full and open competition, and competition advocates. This part does not deal with the results of competition (*e.g.*, adequate price competition), that are addressed in other parts (*e.g.*, Part 15).

Full and open competition requirements exist to prevent unjust favoritism, collusion or fraud in government contracting.[162] FAR sections 6.1 and 6.2 require federal contracting agencies to permit all responsible sources to realistically compete for the contract award. It is through this open contracting that government is able to realize the benefits of competition.

FAR has established a policy statement requiring federal contracting officers to provide full and open competition in soliciting offers and awarding government contracts.[163] This policy requires contracting officers to utilize the competitive procedures in FAR that are "best suited to the circumstances of the contract action and consistent with the need to fulfill the Government's requirements efficiently."[164]

The procedures required under FAR include the use of sealed bids or competitive proposals, unless otherwise permitted.[165] Sealed bids are called for when time permits the solicitation and

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[159] H.R. Rep. No. 861, 98th Cong., 2d Sess., pp. 1422, 1429 (1984).
[160] Id., at sec. 4101.
[161] House Conf. Rep. No. 104-450, p. 965, 104th Cong. 2d Sess. (1996).
[162] *United States v. Brookridge Farm, Inc*., 111 F.2d 461, 463 (10th Cir. 1940); *See, National Waste Recycling, Inc. v. Middlesex County Improvement Authority*, 695 A.2d 1381, 1387 (N.J. 1997) (The purpose of the public bidding requirements is to provide for competition in public contracting and to guard against profiteering, favoritism, improvidence, extravagance, kickbacks and corruption).
[163] 48 C.F.R., Section 6.101.
[164] Id., Section 6.101(b).
[165] 48 C.F.R., Section 6.102(a) and (b).

evaluation of sealed bids, the contract award will be made on the basis of price and price-related factors, it is not necessary to discuss their bids with submitting contractors, and there is a reasonable expectation that more than one sealed bid will be received.[166] If these procedures are not considered appropriate, the contracting officer then is supposed to use competitive procedures or a combination of competitive procedures, such as two-step bidding,[167] or other competitive procedures.[168]

Mr. Levesque's conclusion that the IBEW contracting-out requirements violate FAR is not supported by the facts. Municipal construction contracts that include work covered by the IBEW CBA, which is further subject to the provisions of Article 2.14.4 contracting-out provisions, do comply with competitive procedures. Sealed bids are utilized. All contractors who meet the qualifications for bidding are able to compete for the work. In other words, were these to be considered federal contracts subject to the provisions of FAR, they would meet the requirements of full and open competition.

Restrictions on public contracting are allowable under certain circumstances, and do not necessarily violate the principles of full and open competition. While acknowledging that the full and open competition standard exists to allow government bodies to obtain goods and services at fair and reasonable prices, the United States Comptroller General, in *Ervin and Associates, Inc*., B-279161; B-279162; B-279187; B-279188, April 20, 1998, noted that SBA and 8(a) set-aside solicitations do not in themselves violate the standard. Instead, these are examples of allowable limitations on the principle of full and open competition.

In order to find a violation, it would be necessary to demonstrate that the procuring agency had acted in bad faith. And, to show bad faith, the protester must establish that the agency acted with a malicious and specific intent to injure the protester.[169] The Comptroller noted that, while solicitations for public contracts require full and open competition, they are subject to restrictions and exceptions that are authorized by law.

In its 1998 "*Report to Accompany Principles of Competition in Public Procurements*",[170] the American Bar Association, Section of Public Contract Law, acknowledged that restrictions on contracting may be appropriate when there is a reasonable basis for imposing such restrictive requirements:

> For example, it may be reasonable to impose performance bond requirements even though the bonding requirement may restrict competition and, possibly, even exclude firms with inadequate financial responsibility. *Northern Management Services, Inc.*, B-261424, June 26, 1995, 95-1 CPD Para. 291. Similarly, where a solicitation requirement relates to safety concerns, the provision may reasonably require the highest possible reliability and effectiveness even though the number of competitors may thereby be reduced. *See, Harry Feuerberg & Steven Steinbaum*, B-261333, Sept. 12, 1995, 95-2 CPD Para. 109. In addition, it may not be practical to solicit all known sources

[166] 48 C.F.R., Section 6.401(a).
[167] Id., Section 6.102(c),
[168] Id,, Section 6.102(d).
[169] C*iting, Industrial Data Link Corp.*, B-246682, Mar. 19, 1992.
[170] Report not submitted by the Section for adoption.

> individually, in which case rotating mailing lists may be reasonable. Any provision that restricts competition, however, should be utilized only if necessary to satisfy a reasonable public requirement. *United States v. Brookridge Farm, Inc.*, (conditions or limitations should have reasonable relation to the public need); *see*, *Marlen C. Robb & Son Boatyard & Marina, Inc.*, B-256316, June 6, 1994, 94-1 CPD Para. 351.

In other words, restrictions such as requirements that a contractor be licensed, bonded and insured, or that the contractor demonstrate status as a minority or disadvantaged entity, are permissible. Even greater bars to full and open competition can be allowable, such as when an exigency exists, where sole-source or limited-source solicitations may be appropriate. The nature and limits of the exceptions to competition requirements, however, are policy decisions to be made by the legislative or policy-making authority and not left to the discretion of purchasing officials. Further, these policy decisions should be set forth in the law governing the public acquisitions.[171] That certainly is the case with the Municipality of Anchorage. The policy decision is contained in the CBA, approved by the Assembly. The purchasing officials for the Municipality do not have discretion in whether or not to include the contracting-out requirements of the CBA.

Finally, principles of public contracting dictate that solicitations must contain sufficiently definite terms and requirements, as free from ambiguity as possible, to permit competition on a level playing field.[172] In other words, in order for there to be meaningful competition, contractors must understand the terms and conditions of the solicitation and have the opportunity to submit proposals based on the same terms and conditions as all others competing for the same contract.[173]

> As the American Bar Association, Section of Public Contract Law has noted:
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> The quality of competition can be affected by both the number and quality of competitors, and both will be reduced if prospective vendors lose confidence in the integrity of the competitive system. This means that the rules of the competition for public contracts must be fair, disclosed, and enforced. Preparation of bids and proposals can be an expensive process, and prospective vendors may be unwilling to incur such costs unless there is reasonable assurance that the purchaser will abide by the rules it establishes for the competition.

An examination of the contracting-out requirements of the IBEW CBA show that all contractors are able to compete for Municipal contracts under the provisions of the CBA. Not being signatory to an IBEW CBA does not bar any contractor or subcontractor from competing for these contracts. If they are not a signatory, and the solicitation requires application of the contracting-out language, the contractor or subcontractor may elect to become signatory to a CBA, or it can obtain a letter of assent from the IBEW.

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[171] Id.

[172] *Science Pump Corp.*, B-255803, April 4, 1994, 94-1 CPD, Para. 227; *Grey Advertising, Inc.*, 55 Comp. Gen. 1111 (1976), 76-1 CPD, Para. 325.

[173] *Macro Systems, Inc.*, B-208540.2, Jan. 24, 1983, 83-1 CPD, Para. 79; *Cylink Corp.*, B-242304, Apr. 18, 1991, 91-1 CPD Para. 384; *JG Engineering Research Assoc.*, B-224892.2, March 3, 1987, 87-1 CPD, Para. 239.

Understandably, this imposes an additional step for contractors and subcontractors who choose to compete for these projects. However, in all solicitations, there are threshold requirements which must be met for consideration for a contract with the Municipality. As noted above, these restrictions may include, for example, licensing, insurance and bonding requirements. In the case of a project for a Municipal department covered by the IBEW CBA which involves covered electrical work under Article 2.14.4, the contractor or subcontractor either must be signatory to an IBEW CBA or possess a letter of assent from the IBEW.

By meeting these threshold requirements, the contractor or subcontractor becomes eligible to bid on the work. On the other hand, if the contractor or subcontractor chooses not to be licensed and bonded, or chooses to ignore the union signatory/letter of assent requirement, or any other material pre-condition of the bidding process, the contractor or subcontractor will not be considered eligible for an award of the contract or subcontract.

CONCLUSION:

In the absence of implementing code or more detailed guiding history from the Charter Commission, we conclude that Charter §13.06(a) requires the mayor to report to the Assembly when he knows to a reasonable certainty that revenues will be less than appropriations for the fiscal year. The Charter provision expects revenue forecasting so that an "early warning" is given to the Assembly. What constitutes a shortfall worth reporting and when the reporting should occur are determined by the circumstances, including the risks presented to the Municipality's financial well-being. We conclude that Mayor Begich knew that revenues for the 2008 and the 2009 budgets were reasonably certain to be less than appropriations and that the shortfall would have a significant impact on the Municipality's financial well-being, but did not timely report this to the Assembly.

We stated at the beginning of this report that we understand our interpretation of what is required is not unassailable. Presuming our standard expects too much of a Mayor and the conclusion is reached that this Charter provision was not violated, we nevertheless conclude that the failure to discuss with the Assembly the extent of the revenue shortfall during the latter half of 2008 is not within the range of competent administration of the Municipality's budget.

Given the current circumstances, there are fewer remedies available today than might have been in 2008. There is no basis under principles of contract law that would justify the rescission of the 2008 IBEW or the APDEA CBAs approved by the Assembly. Rescission is not available on the basis of unilateral mistake or error on the Assembly's part. And, relief from the CBAs is not available based on lack of fund certification, given that this certification is not required, and no such certification could have been provided.

The IBEW CBA is not subject to rescission or reformation on the basis of violation of federal contracting standards specifying full and open competition. No contractor or subcontractor is precluded from bidding on any Municipal contract by operation of the contracting-out requirements of the CBA. All contractors and subcontractors who desire to do business with the Municipality compete on the same basis. There are no hidden preferences, bars to participation by any contractor who meets these requirements, or bad-faith or otherwise prohibited restrictions on full and open competition.

The contracting-out requirements of the IBEW CBA have the force of law and policy and do not violate principles of full and open competition. The Municipality is legally bound to comply with the lawful terms and conditions of the IBEW CBA. We also note that both contracts contain severability clauses.

Ratification by the Assembly has rendered further attempts to revisit the CBAs on the basis of the failure of Mayor Begich to disclose financial information or on the basis of the absence of material terms during the initial approval process, legally unsupportable.

Finally, we note that even if the Assembly had been fully informed regarding the state of municipal finances, this does not lead to the conclusion that the CBAs would have ended up different than they did. The Assembly cannot renegotiate the terms; it could not have imposed lower wage increases, for example. They could have rejected the contracts, but it is not pre-ordained that the process from that point, including the possibility of arbitration, would have produced a different result.

We recommend the Assembly and the Sullivan Administration amend the Code to fully implement the Charter provision to avoid any further debate on what is expected of the executive branch under §13.06(a).[174]

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[174] We note that the general penalty provisions in AMC 1.45 do not apply to violations of the Charter: 1.45.010 General penalties. A. Every act prohibited by this ***Code*** is unlawful. (emphasis added) *Code* is a defined term under AMC 1.05.020 and does not expressly include Charter provisions.