

**IV. "FISCAL GAP" --
PROBLEM AND SOLUTIONS**

IV. "FISCAL GAP" - PROBLEM AND SOLUTIONS

Developed in 1990, this section is intended to identify corrective actions to resolve the Fiscal Gap facing the Municipality. The term Fiscal Gap is derived from the shortfall that exists when desired expenditures are greater than available revenues. The Administration's recommendation to resolve the Gap is contained later in this section.

PROCESS

Many of the factors directly impacting the model have been reviewed and analyzed by the administration, department directors, and the Fiscal and Economic Trends Committee. Input from these various groups provided a strong base for the planning process involved in the fiscal gap model.

"FISCAL GAP"

Per Figure 4-1, the primary Fiscal Gap estimate is that amount which includes Mandated New Requirements. In addition to the primary Fiscal Gap amount, High Priority New or Increased Discretionary Programs/Services and the Unfunded Police and Fire Retiree Medical Benefits have also been shown.

The New Requirements have been developed by each of the departments in General Government. The direction given to these departments centered on providing realistic new requirements that would impact the operating budget during the 1994 to 1999 time frame. All cost information reflects expenditures over the 1993 approved budget level, adjusted for first quarter revisions and one-time expenditures.

The New Requirements section of the Fiscal Gap Report is divided into several sections, which are outlined below:

1. Legally Mandated Services -- This category encompasses services or programs mandated by Federal, State, or Municipal law, statute, ordinance, code, or regulation. The components of this category should receive priority funding because of the implications of non-compliance.
2. Additional costs of existing programs/services -- This category centers on the additional cost of current contracts or programs, other than inflationary increases, needed to provide the same level of service.

3. High Priority New or Increased Programs/Services -- This category entails the increased discretionary programs/services that would be beneficial to the Municipality to increase. This is not a wish list, but a well developed management plan for the effective functioning of the various Municipal departments.

In order to cover the costs of certain mandated new requirements, it is anticipated that the city will receive State grant assistance or voter approved bonds in the following areas:

- Underground Storage Tanks
- National Pollution Discharge Elimination System (NPDES)
- Americans with Disabilities Act (ADA)

Additionally, certain High Priority new or increased programs/services will comprise the 1994 Legislative Program for the Municipality. Some of these key projects include:

- Building Maintenance (deferred and ongoing)
- Road Rehabilitation
- Park and Trail Compliance with ADA

By far the largest component of New Requirements would be the potential unfunded medical liability for Police and Fire retirees. This \$21.6 million number is shown below the line, but by no means is it any less important. An actuarial valuation as of January 1, 1991 of the future expected benefit payments under the Anchorage Police and Fire Health plan is \$1.3 billion. The present value of benefits -- over \$159.7 million -- resulting from an updated valuation of the Municipality's Police, Fire and command officers Retiree Health Plan originally estimated by William M. Mercer, Inc., and confirmed by Martin E. Segal Company. In other words, \$159.7 million plus interest at an annual rate of 8% would cover the future expected payments under the plan.

All assumptions for revenues at Figure 4-1 have been delineated within parentheses next to the revenue source. Wages and benefits are increasing per existing contractual obligations and other services increasing at a rate of 5.9% during the future years. With recent projections on health care benefits indicating potential increases of 9-11% in 1994, the expenditure portion is probably conservative.

Figure 4-1

"Fiscal Gap"
(In \$ Millions)

	1994	1995	1996	1997	1998	1999
REVENUES						
Federal Revenues (0%)	\$ 1.10	\$ 1.10	\$ 1.10	\$ 1.10	\$ 1.10	\$ 1.10
State Revenues (-5% after 1994)	30.62	29.09	27.63	26.25	24.94	23.69
Local Revenues (2%)	46.77	47.70	48.65	49.63	50.62	51.63
Property Taxes (Constant + New Construction)	114.25	115.45	116.65	117.85	119.05	120.25
Fund Balance Applied (2% Prior Yr. Expend.)	7.02	4.28	4.48	4.69	4.91	5.15
IGC's (+5.2% after 1994)	14.13	14.86	15.63	16.45	17.30	18.20
TOTAL REVENUES	\$213.88	\$212.48	\$214.15	\$215.96	\$217.92	\$220.02
EXPENDITURES						
Personal Services (5.9% After 1994*)	\$125.46	\$132.86	\$140.70	\$149.00	\$157.79	\$167.10
Debt Service	23.29	23.29	23.29	23.29	23.29	23.29
Other (4%)	65.14	67.75	70.46	73.28	76.21	79.25
TOTAL EXPENDITURES	\$213.88	\$223.89	\$234.44	\$245.56	\$257.28	\$269.64
FISCAL GAP (Reference Figure 3-2)	\$ 0.00	\$ 11.41	\$ 20.29	\$ 29.59	\$ 39.36	\$ 49.62
NEW REQUIREMENTS - INCREASES TO THE GAP						
Legally Mandated Services:						
Employee Relations -- ADA & ISTE A Compliance	\$ 0.00	\$ 0.02	\$ 0.02	\$ 0.02	\$ 0.02	\$ 0.02
Employee Relations -- New Labor Contracts	0.00	0.22	0.22	0.66	0.22	0.22
H&HS - ADA (Supplemental Trans. Vans)	0.00	0.05	0.10	0.14	0.14	0.14
Asbestos Removal -- P&FM	0.00**	0.64	0.00	0.00	0.00	0.00
Handicapped Access (ADA) -- P&FM	0.00**	2.90	0.00	0.00	0.00	0.00
Underground Storage Tanks -- P&FM	0.00**	1.00	0.20	0.15	0.15	0.00
PW -- EPA Non-Point Discharge Regulations	0.00	0.00	0.07	0.17	0.28	0.40
Emergency Mgmt -- ADA & Training Requirements	0.00	0.03	0.02	0.02	0.02	0.02
Cultural & Rec Svcs -- Required ADA	0.00**	0.21	0.14	0.14	0.14	0.14
Subtotal	\$ 0.00	\$ 5.27	\$ 0.77	\$ 1.30	\$ 0.97	\$ 0.94
Additional Cost of Existing Programs/Services:						
Increased Utility Charges to General Govt.	\$ 0.00	\$ 0.01	\$ 0.01	\$ 0.02	\$ 0.02	\$ 0.02
Police/Fire Retiree Medical Pay-As-You-Go Costs	0.00	0.87	0.58	0.63	1.43	0.85
Subtotal	\$ 0.00	\$ 0.88	\$ 0.59	\$ 0.65	\$ 1.45	\$ 0.87
FISCAL GAP Before Addition of Discretionary New Requirements or Potential Unfunded Police/Fire Retiree Medical Liability	\$ 0.00	\$ 17.56	\$ 21.64	\$ 31.54	\$ 41.78	\$ 51.43

* Applicable step and longevity increases plus annual salary increases based on assumed inflation rate of 3.8%. Annual salary increases are shown in the outyears for purposes of illustration of potential fiscal gap impacts only and are not necessarily supported by the Administration.

** Funding will be pursued through 1994 State Legislative Capital grants and/or through April 1994 bonds. Assuming 1994 State grants and/or April 1994 bond dollars are not forthcoming, the 1994 deferred costs will need to be funded as part of the 1995 General Government Operating Budget.

NOTE: Due to rounding, amounts shown in Figure 4-1 may not total exactly.

	1994	1995	1996	1997	1998	1999
High Priority New or Increased Discretionary Programs/Services:						
P&FM -- Deferred/Ongoing Building Maint.	\$ 0.90	\$ 0.90	\$ 0.90	\$ 0.90	\$ 0.90	\$ 0.90
P&FM -- Replacement of Heavy Equipment	1.20	0.00	0.00	0.00	0.00	0.00
Employee Relations -- Add'l Staff Support	0.22	0.23	0.23	0.23	0.23	0.23
Pub. Works -- Deferred/Ongoing Maintenance	11.01	12.28	13.40	13.28	13.28	13.28
Finance	0.68	0.68	0.68	0.68	0.68	0.68
Transit -- Repair/Maint -- Older Vehicles	0.25	0.20	0.20	0.00	0.00	0.25
Cultural & Recreation	2.28	2.85	4.16	3.03	3.17	3.18
Fire -- Replace/Expand Equipment Inventory	2.07	2.18	2.30	2.42	2.55	2.69
Emergency Mgmt. -- Maintain/Upgrade Equip.	0.05	0.03	0.03	0.03	0.03	0.02
Subtotal	\$ 18.66	\$ 19.34	\$ 21.89	\$ 20.57	\$ 20.83	\$ 21.23
Total New Requirements	\$ 18.66	\$ 25.49	\$ 23.25	\$ 22.51	\$ 23.25	\$ 23.05
TOTAL FISCAL GAP with Increases	\$ 18.66	\$ 36.90	\$ 43.54	\$ 52.11	\$ 62.61	\$ 72.66
Police/Fire Retiree Medical Benefits (Based on 40-Year Partial Advance Funding)	\$ 21.60	\$ 21.60	\$ 21.60	\$ 21.60	\$ 21.60	\$ 21.60
Fiscal Gap Including Unfunded Medical Liability for Police/Fire	\$ 40.26	\$ 58.50	\$ 65.14	\$ 73.71	\$ 84.21	\$ 94.26

Figure 4-2
Total Fiscal Gap
"Most Likely Case"

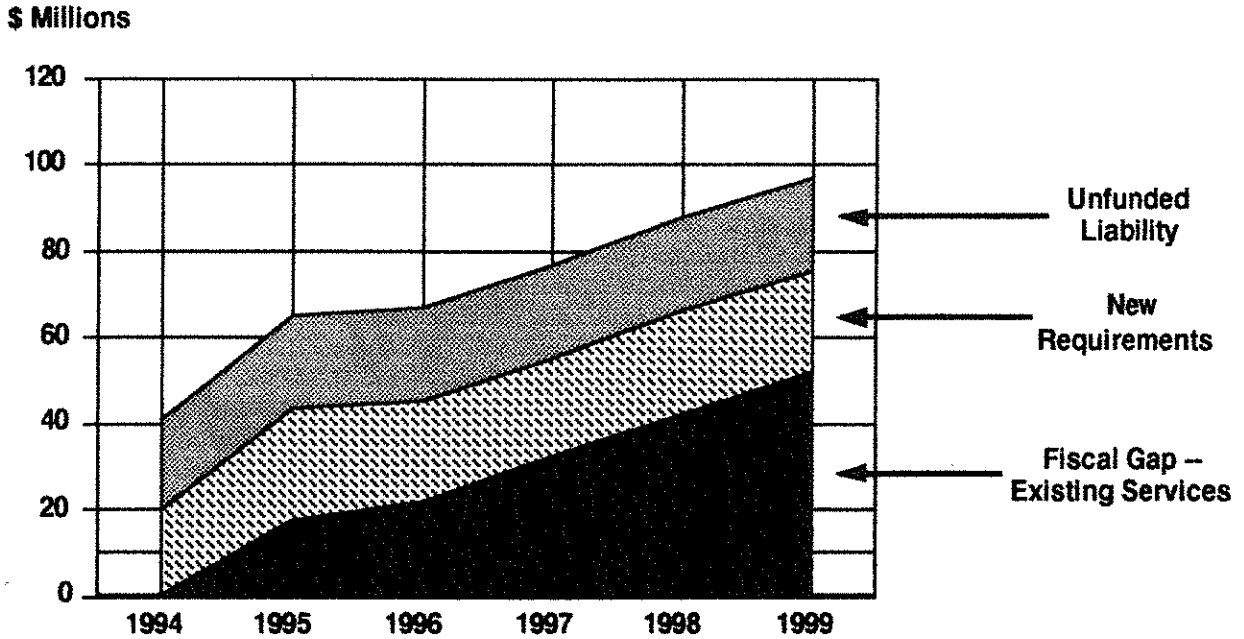
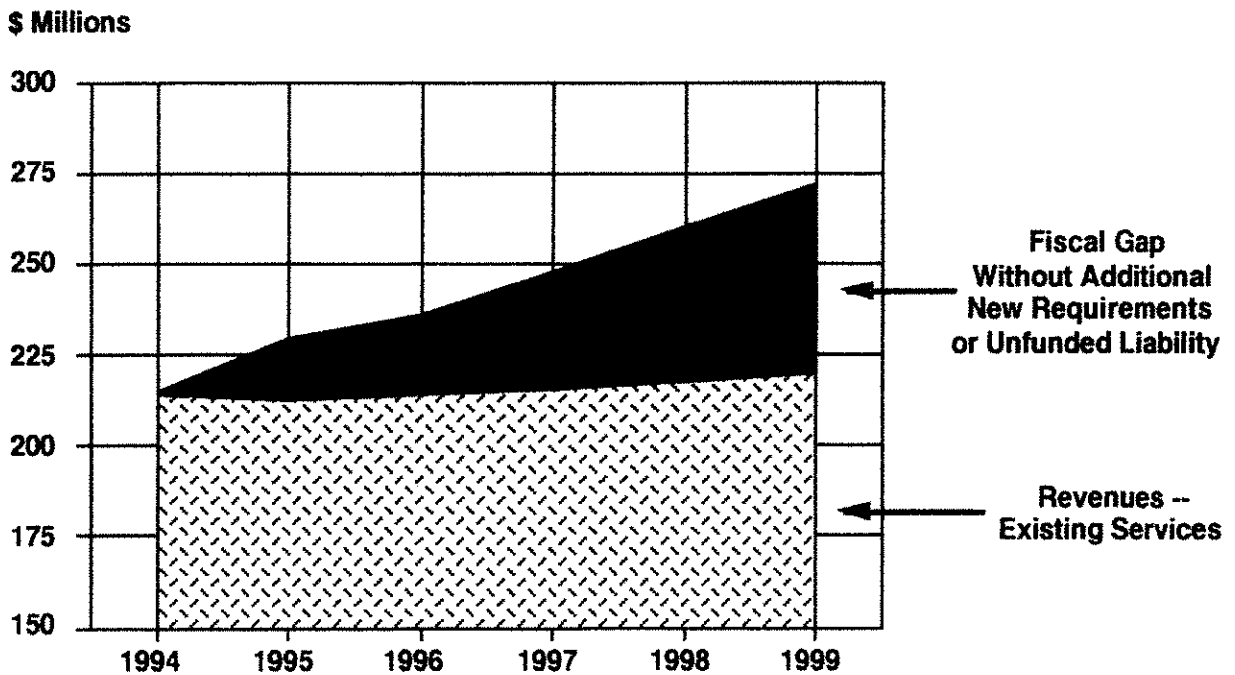


Figure 4-3
Current Level Expenditures
Minus Expected Revenues



FISCAL POLICY ANALYSIS

This portion of the Fiscal Trends document explains the preliminary policy analysis related to the evaluation of potential Fiscal Gap solutions.

In order to develop a comprehensive plan to solve the Fiscal Gap, it will be necessary to find agreement on the solution option that would resolve the projected gap. The feasibility of the most desirable public policy solution options should be assessed as the final step in the process.

With the Fiscal Gap identified, the next logical step is the establishment of proposed solutions necessary to remedy the problem. Policy options include the following categories:

- Compensation Concessions
- Utility Policy
- Service and Program Adjustments
- New Revenues

These options are presented for analytical purposes. The Administration does not support higher utility rates, taxes or user fees beyond those to be proposed in the 1994 Operating Budgets.

Compensation Concessions

Salaries - Labor contracts for all Municipal labor groups are currently scheduled to expire in 1994. Labor concessions from the various bargaining units would reduce the threat of corresponding departmental reductions. Wage freezes have been successfully negotiated over the past year for most all labor groups, with the exception of the IBEW and Fire unions.

Cost of Living Adjustments (Benefits) - Inflationary increases and projected experience factors related to health benefits have not been included in the Fiscal Gap model beyond 1994. Should unfavorable changes occur, they would increase the Fiscal Gap.

Police and Fire Retiree Medical Benefits - An actuarial valuation as of January 1, 1991 of the future expected benefit payments under the Anchorage Police and Fire Retiree Health Plan is \$1.3 billion. An April 1993 update of the actuarial valuation estimates the present value of benefits related to the Municipality's Police and Fire retiree health plan at \$159.7 million. In other words, \$159.7 million plus interest at an annual rate of 8% would cover the future expected payments made under the plan. This amount equates to a \$21.6 million a year (FASB 106) potential expense based on a 40-year partial advance funding. The 1994 solution to the Gap does not account for any

funding of this potential liability, yet the need still exists and should be resolved. Funding of the full actuarial liability will likely be mandated by the Government Accounting Standards Board (GASB) by 1996.

Utility Policy

Sale of ATU - One of the options available for reducing a fiscal gap is for the Municipality to sell ATU and use some of the revenues to assist in offsetting a Fiscal Gap. If the terms of sale were similar to those proposed during the previous sale attempt, the Municipality would benefit as follows:

- \$150 million of outstanding debt at ATU would be eliminated.
- Invest \$100 million for retiring general obligation debt, which has a corresponding impact on the taxpayer.
- Establish a permanent fund for approximately \$150 - \$200 million. The interest earnings after inflation-proofing are approximately \$3.3 - \$4.4 million annually, which could be used to close the Fiscal Gap.

In addition, this solution would provide a source of funds for critical priorities upon approval of the voters.

Sale of Other Utilities - ML&P appears to be the only other feasible candidate and would produce an estimated permanent fund addition of \$50 million.

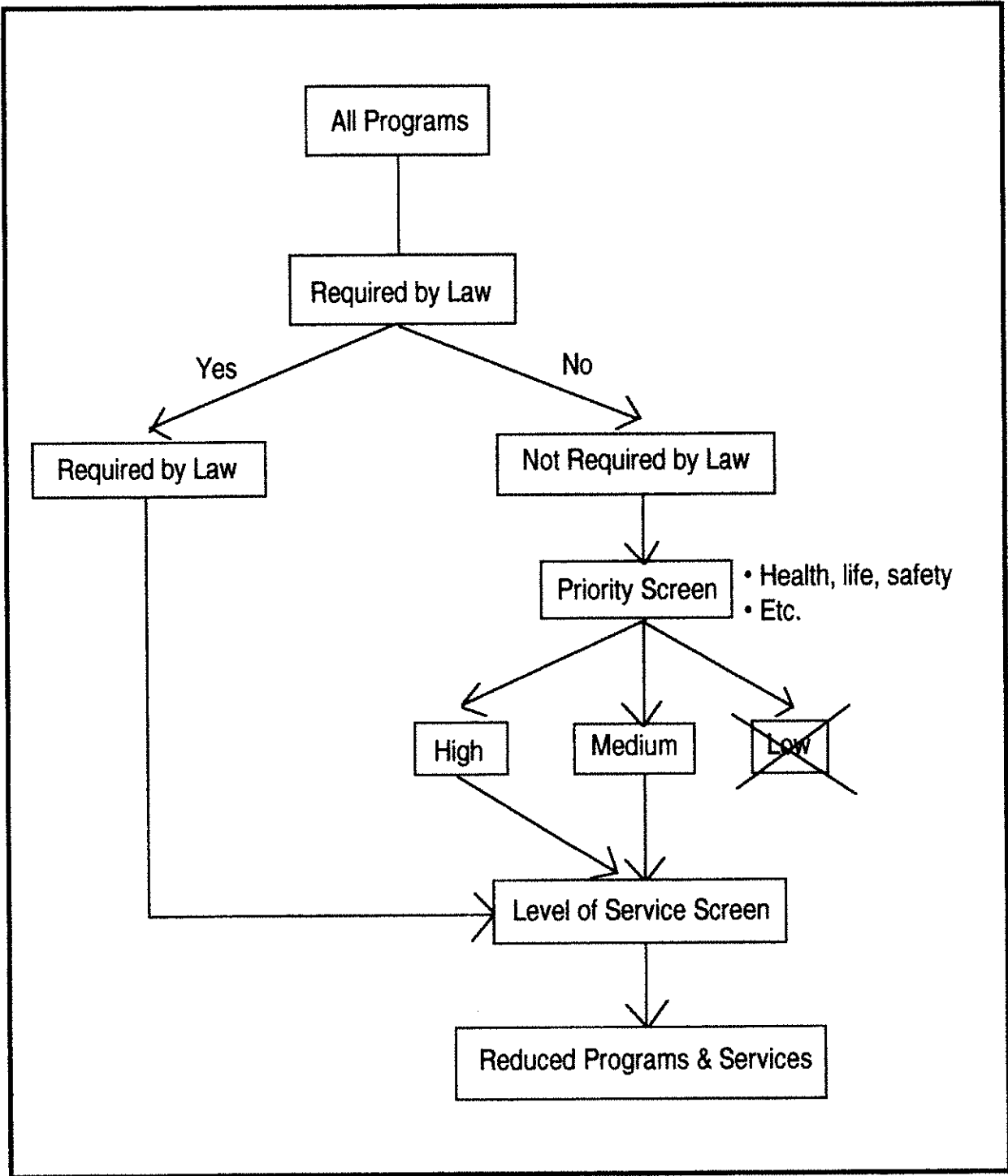
Increased Utility Revenue Distribution - These amounts are directly dependent on the Municipality's dividend policy and the Utilities' ability to pay. Projected utility rates will be affected by the anticipated URD's.

Service and Program Adjustments

Service and Program Reductions - This category will encompass dollar savings which will vary with the assumptions utilized in determining service/program priorities and desired levels of service.

Internal Management Review - A current review program began May 1993. In general, this review is intended to find ways to save money (efficiency) and to make operational improvements (effectiveness). Specific recommended actions may include deletions, reductions, consolidation, reorganization, elimination of duplication, privatization, operational improvements, new or additional cost saving technology, and other alternate, less costly ways of performing services.

The model on the following page was utilized in establishing priorities for services and programs.



New Revenues

State/Federal Assistance for Mandated Programs - More emphasis should be put on assistance with State or federal mandated requirements.

Major Repairs and New Requirements - Additional State grants and bond funds should be sought to provide more funding for major repair and maintenance of the existing infrastructure and for new, mandated requirements.

Exemption Program for Senior Citizens and Disabled Veterans - The Municipality could reduce taxes to existing taxpayers if we were given a local option for the property tax exemption program and if we amend the Municipal Code to provide a needs-based or smaller exemption. The Municipality is anticipating State funding at approximately 12% for 1994. This option would be a redistribution of taxes rather than additional money.

User Fees - This category would entail an increase to the fee structure imposed by the Municipality on its users. Generally, the Administration does not recommend this as a new revenues solution.

Property Tax - This solution would incorporate taxing the maximum allowed under the cap. Generally, the Administration does not recommend this as a new revenues solution.

Heritage Land Bank - The opportunity for sales of land to private developers is expected to increase significantly in the next several years. As real estate market prices continue to rebound from the late 80's, the Municipality can begin to generate new revenues from land sales as well as new property tax revenue to support existing government services.

Re-distribution of Hotel/Motel Tax - The Municipal Charter requires 50% of the collected Hotel/Motel tax to be used in promoting tourism. Since the Charter does not specify the recipient, some portion of the 50% collected could be re-distributed to support Municipal agencies whose functions directly promote tourism (i.e., downtown flowers, parks, trails, etc.)

Additional Taxes - This solution has various possibilities for generating a range of revenues. It is presented here for analytical purposes. The Administration does not support new taxes at this time without voter approval. Note that voters rejected by a 2-to-1 margin the sales tax proposition which appeared on the April 1993 ballot. Examples of additional taxes are as follows:

- Alcohol Tax - Current revenue estimates from a retail alcohol sales tax are \$1 million annually per 1 percent of tax.

- Sales Tax - \$10 million annually per 1 percent of sales tax. This current estimate applies to retail sales only and assumes certain exemptions (i.e., food, prescriptions, professional services, etc.).
- Hotel/Motel Tax - Currently the tax of 8% generates approximately \$6 million. Therefore, an increase from 8% to 10% could be expected to generate an additional \$1.5 million in revenues without any real increase in administration costs.

PROPOSED SOLUTIONS TO THE 1994 FISCAL GAP

The \$22 million projected Fiscal Gap in 1994 has virtually been eliminated, assuming the assumptions regarding revenues, expenditures, and proposed solutions occur. Figure 4-4 is an explanation of those solutions brought forth by the Administration to eliminate the 1994 Gap as reflected in the Administration's Proposed 1994 General Government Operating Budget.

Figure 4-4

1994 Fiscal Gap Solutions (\$ Million)

FISCAL GAP PRESENTED AT MAY 18 ASSEMBLY WORKSESSION	\$22.1
<u>Increase/(Reductions) to Fiscal Gap:</u>	
• State Revenues (Governor Not Reducing Legislative Appropriations)	(9.7)
• State Revenue Sharing Additional Reduction Due to Minimum Entitlements (1993/94)	0.8
• 1994 Savings from Two-Year Wage Freeze	(4.2)
• Heritage Land Bank Fund Balance	(2.5)
• Self Insurance Fund Additional Fund Balance	(2.3)
• Additional Applied Fund Balance from 1992 Savings	(2.0)
• Increased Auto Taxes and Tobacco Taxes Revenues	(0.3)
• Captain Cook Parking Garage "Balloon Payment"	(0.3)
• Additional Property Taxes on New Construction	<u>(0.3)</u>
REVISED GROSS FISCAL GAP (Unfunded Current Service Levels)	\$ 1.3
• Programs/Services Transferred to Grant Support	(0.2)
• Reduced Costs of Providing MISD Computer Services to ATU	(0.3)
• Funded High Priority Discretionary New Service Level Deemed by Department Directors to be of Higher Priority Than Unfunded Current Service Level	(0.3)
• Reduce Lower Priority Costs/Services	<u>(0.5)</u>
1994 FISCAL GAP	\$ 0.0

Funding for certain mandated new requirements for 1994 will be pursued through 1994 State Legislative Capital grants and/or bond propositions. To the extent this is not successful, the 1994 deferred costs will need to be funded as part of the 1995 General Operating Budget and will increase the 1995 fiscal gap accordingly.

Again, the Administration's Proposed 1994 General Government Operating Budget does not fund the potential Police/Fire retiree medical liability at this time, but we continue to recommend that this problem be resolved by the Assembly, and not by an arbitrator.

OTHER/LONG-TERM SOLUTIONS TO THE FISCAL GAPS BEYOND 1994

A number of possible solutions exist, in addition to those mentioned above, where implementation and affect most likely would reduce the Fiscal Gap projected beyond 1994. Below is a short list of suggested long-term solutions to the Fiscal Gap:

- 1994 labor concessions
- Sale of utilities (i.e., ML&P and ATU)
- Privatization of certain functions
- Consolidation measures (e.g., School District)
- Efficiency measures
- Heritage Land Bank sales of land
- On-going internal management review program
- New taxes are not supported by this Administration until three primary goals are achieved:
 - (1) labor costs brought in line,
 - (2) maximum use made of our resources, and
 - (3) the public convinced that goals #1 and #2 have been achieved.