Finance Department
Joseph G. Newlin
Finance Director
jnewlin@cityofoxford.org

(513) 524-5228 office
(513) 524-7298 fax

INTEROFFICE MEMORANDUM

DATE: November 13, 2020

TO: City Council

FROM: Joe Newlin

RE: 2020 Drawing Down General Fund Balance Analysis

Cc: Doug Elliott, Department Heads, Heidi Hill, Chris Conrad, Ben Mazer

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During the budget workshop Jason ask what I was comfortable with drawing down the General Fund balance. In this memo I will provide backup to my position.

For many years now during the budget work session I have provided an analysis to City Council including: “City of Oxford General Fund Revenue Expenditure Trends” worksheet, “Declining Revenue Streams - General Fund Chart”, “City of Oxford General Fund Declining Revenue Trends” worksheet, “City of Oxford General Fund Revenue Trends” worksheet, “General Fund Revenue Trends” chart, “City of Oxford General Fund Revenue Trends” worksheet, “City of Oxford General Fund Expenditure Trends” worksheet. This year I included “Street Fund Ending Balance”, “City of Oxford General Fund Revenue Expenditure Trends” worksheet from the 2020 budget, “City of Oxford General Fund Revenue Expenditure Trends Recession in 2021” from the 2020 budget. Here is the link for this year’s budget work session:

https://www.cityofoxford.org/sites/default/files/finance/2021%20Budget%20Notes.pdf

During this past year I have sent out updates to Council on issues that will affect the City’s finances such as:

https://www.cityofoxford.org/sites/default/files/finance/Council%20Updates%20on%20Revenue%20Issues.pdf

https://www.cincinnati.com/story/news/2020/11/08/ohio-income-taxes-covid-work-from-home/6185682002/

All of this information is meant to inform Council on issues that I look at when I do my analysis of both short term and long term health of the City’s finances.

https://www.cityofoxford.org/sites/default/files/finance/2020%20General%20Fund%20Ending%20Balance.pdf

In the link above are four graphs, the first "General Fund Ending Balance". This chart compares the General Fund Ending Balance, the amount transferred out of the General Fund, the General Fund Ending Fund Balance as a percentage of Operating Expenditures and Transfers as a Percentage of General Fund Ending Balance. The work sheet that follows is the source data for this graph and I will now explain the major variances. First the increase in operating expenditures jumped $629,259 between 2006 and 2007. $512,649 or 81.5% of the increase is in three areas Police and Fire expenditures make up $454,949 or 88.7% of the increase. Personnel expenditures accounted for $314,651 of the $454,949. In the budget in 2007 and 2008 an additional Sargent, Public Safety Assistant, Dispatcher, Property Manager and Assistant Fire Chief were added. $57,700 of the $629,259 is attributed to paying the Visitors Bureau out of the Community Assistant Department. This practice was an accounting nightmare so in 2010 it was paid directly out of the Hotel & Convention Tax Fund rather than transfer the money from the Hotel & Convention Tax Fund to the General Fund and then paying the VCB from the General Fund. In the years 2008 – 2010, the increase of expenditures are due to ramping up of the Fire Department to 24 hour coverage and our settlement for the Western Knolls property lawsuit. In 2008 we payed $1,752,021, 2009 we paid $567,097 and in 2010 we paid $595,000.

Next the Percentage of Transfers to the General Fund Ending Balance. In 2002 $1,950,000 was transferred to the Capital Improvement Fund and in 2003 $1,800,000 was transferred to the Capital Improvement Fund. From large Capital Improvements made after these transfers I imagine they were made to fund the US 27 North road improvements. In early 2008 a $2,000,000 was made to the Capital Improvement Fund. Looking at the 2008 budget this was done to cover projects in the 2008 budget in particular the US 27 North Road Improvements Phase III. City Council made a deliberate decision to pay for the improvements made to the old Municipal Building and a new undetermined site for the Police Division, City Manager, Clerk of Council, Human Resources, Planning and Community Development, Engineering and Finance. This was a long term goal of the City. Around the same time in 2009 the Great Recession started. Under the direction of the City Manager spending was curtailed including not filling positions when the occurred, limiting operational expenditures and limiting transfer for Capital Improvements and Equipment. As you can see the General Fund balance started to grow in 2009 as a result of these changes. We always budget revenues conservatively and Department Head always control their expenditures. This plan worked despite the fact that the State eliminated Inheritance Taxes and cut Local Government Funding. As the economy started to recover we slowly started to fill open positions and if warranted increased operational expenditures if the need existed. In 2013 we started to transfer funds to the Municipal Facilities Improvement Fund to move forward on the project. First to purchase the old Lane Library and start the planning stages for the remodeling of both the old Municipal Building for the Police Division and the Lane Library building for the new Municipal Building. The design phase determined that this was the most economical way to proceed. In 2015 $1,000,000 was transferred to the Municipal Facilities Improvement Fund, in 2016 $1,500,000 was transferred, in 2017 $3,400,000 was transferred and in 2018 $1,700,000 was transferred. By 2019 both buildings were complete and everyone settled into the new work spaces.

Next the Percentage of General Fund Ending Balance to Operating Expenses. As expected over a 21 year time frame, expenses will increase. The average percentage over the time frame is 68.17%. One of the main points to take from this is inversely related to the amount of money transferred out of the General Fund. The more you transfer out the fund balance will decrease and the amount of the fund balance compared to operating expenses will then decrease. In 2021 the average is 58.77%. For comparison it was higher in 2001 when it was 64.04%. Some of the main drivers is we will finally added one new Patrol position to help cover the School Resource Officers position since the County Sheriff's Department is no longer filling the position at Marshall Elementary School. We do get some relief from the Talawanda School District paying a portion of salaries of the School Resource Officers position. Also Body Cameras are now an annual cost to the City at a budgeted amount of $40,000.

The next graph "General Fund Revenue & Expenditures" compares total operating expense and total operating revenue. The work sheet that follows is the source data for this graph. This graph is pretty straight forward it's a measurement of how much the operating revenue is dedicated to covering operating expenditures. As you can see the average over the 21 year period is 77.11%. By eliminating the 2008 – 2010 time frame, due to unusually high expenditures related to the ramp up to 24 hour Fire & EMS operations and the high 90.78% and the low of 62.54% the average is 75.24%. This shows expenditures are nearing the revenue available to cover them. This will mean less money is available to transfer out for Capital Improvements and Equipment. This is due to lower revenues projected due to the effects of COVID-19 on income tax and hotel taxes.

The next graph "Income Tax Revenue" shows income tax revenues from 2005 thru the 2021 budgeted figure. The work sheet that follows is the source data for this graph. The Great Recession reared its ugly head in 2008 and income receipts dropped for three consecutive years bottoming out in 2011. In total there was a $387,469 or 5.48% drop from 2007 thru 2011. It took another two years to recover at $7,284,301. We enjoyed six years of steady growth topping out at $9,351,198 in 2019. In 2021 the budgeted amount is expected to drop $721,198 or 7.71% compared to 2019. This is a major decrease and it's unknown at this time how long the downturn will last and again return the 2019 levels.

The final graph "General, Capital Equipment & Capital Improvement Funds Ending Balances" is a stacked bar chart blue – General Fund, green – Capital Improvement Fund and red – Capital Equipment Fund. This chart represents a snapshot of the ending balances that are an essential part of the review process the City goes through with Moody's when we go out to issue debt. The next three sections are directly from the three Moody's reviews that I have been part of since beginning working for the City in May of 2008. I was also involved in three Moody's presentation when I worked for the City of Avon Lake. There the Fund balances they looked at were the General Fund, Capital Improvement and the Income Transfer Fund. Income taxes were placed in the Income Transfer Fund and split 70% General Fund, 25% Capital Improvement Fund and 5% Sewer Replacement Fund by their City Ordinance. Each year so much was budgeted to be transferred out and if revenue exceeded the budgeted transfers the balance in the Income Transfer fund would increase with 70% of that balance belonging to the General Fund. Please review the three Moody's ratings below and following these I will state my recommendations.

June 12, 2009 Moody's Investors Service Rating – Aa3 Rating to the City of Oxford's (OH) $2.58 Million GO Refunding Bonds, Series 2009:

<u>Well-managed finances supported by ample reserves; stable income tax base</u>

Moody's believes the city's well-managed financial operations will remain healthy due to the presence of ample reserves, the expectation of balanced operations in FY09 and the city's prudent management practices. The city has a history of maintaining healthy reserves and reporting operating surpluses despite substantial annual transfers out of the General Fund to the city's capital funds. Unaudited FY08 results, show a modest increase in GAAP basis balances with an ending General Fund balance of $6.2 million or an ample 44% of General Fund revenues. In FY08, the city purchased land as a result of a lawsuit settlement for approximately $2 million through transfers into the General Fund from the Capital Improvement Fund skewing the city's FY08 operating statement. The city is currently projecting a General Fund surplus in FY09 of approximately $500,000. The city has been able to maintain and grow General Fund reserves despite transferring out $1 million or more annually to its capital improvement fund and capital equipment fund. In FY08, the city recorded a fund balance in the Capital Improvement Fund of $6.9 million and maintains a reserves of nearly $1.2 million in the Capital Equipment Fund; the city can transfer unreserved funds back to the General Fund for operating purposes or reduce annual transfers out of the General Fund should operating pressures arise.

Oxford, like most Ohio municipalities, is reliant on economically sensitive income tax revenues. In FY08, the city's municipal income tax accounted for 59% of General Fund revenues. Management budgeted for a 4.3% decline in income tax collections in FY09, but is currently experiencing essentially flat collections from FY08 levels. The city has averaged a 5.2% annual increase in income tax revenues over the past five years. Better than forecasted income tax receipts along with conservative estimates of other revenue sources and a proven track record of underspending budgeted appropriations account for the city's anticipation of an operating surplus in FY09. Moody's notes that income tax receipts are concentrated, with over 50% of revenues generated by Miami University (rated A 1 with stable outlook). However, concentration concerns are mitigated by the stable nature of the university's operations which provide a measure of protection from economic cycles and the stability of the district's other large taxpayers which include a local hospital.

Modestly sized tax base benefits from institutional presence of Mimi University of Ohio, income levels and tax base size skewed by university presence

Moody's believes the city's modestly sized tax base will remain stable and continue to experience modest growth due to the presence of Miami University of Ohio and the availability of land for future development. The city's $894 million tax base is located in rapidly growing Butler County (GOLT rated Aa2) 35 miles north of the Cincinnati (rated Aa1 with stable outlook) metro area and near Dayton (rated A1 with stable outlook). While the city is located in a portion of the county that has not historically experienced the same levels of rapid growth as eastern sections of Butler County, the city expects that transportation improvements that are underway and planned for the future will expand development potential. Officials report that university owned property, accounts for a sizable amount of tax exempt property which, if added into the city's tax base, would bring full valuation to nearly $5 billion. The city recently annexed approximately 46 acres and has future annexation opportunities tied to the city's ability to provide utilities to surrounding townships allowing ample room for growth in both the north and south as growth, which is expected to continue as medium to long term transportation infrastructure projects are completed. Though near term growth has slowed after the city experienced a 17% increase in assessed valuation in 2009 following a reappraisal, the city does not report any material foreclosure trends.

Despite Butler County's rising unemployment rate (9.1 % in March 2009) which essentially matches the national rate, Oxford's employment base has remained stable. Miami University is the city's largest employer with 3,500 employees, and does expect modest layoffs this summer (approximately 200 positions are expected to be reduced). The city estimates that the effect on municipal income tax receipts will be manageable and account for $158,000 in lost revenues. While the city's income levels are well below average with per capita income at 58% of the state, Moody's recognizes that the large student population of approximately 16,000 full-time students, or over 70% of the city's estimated population, skews income levels downward. Median family income and median home values are both above average, more accurately reflecting resident income levels and the desirability of the community.

January 12, 2011 Moody's Investors Service Rating – Aa2 Rating to the City of Oxford's (OH) $3.46 Million GO Refunding Bonds, Series 2011:

Strengths

- Strong institutional presence with Miami University which has provided relatively consistent income tax receipts and a growing population base.
- Healthy General Fund reserves that have totaled at least 40% of General Fund revenues since fiscal 2006.

Challenges

- Income tax base concentration in the university, the area’s largest employer, which may have a negative effect on the city’s financial position should the university reduce operations.
- Potential reductions in state aid for the city and the university as the State of Ohio considers scaling back local government and higher education funds in the upcoming state fiscal year.

March 19, 2019 Moody’s Investors Service Rating – Aa2 rating to the City of Oxford, OH's $7.4 million Various Purpose Bonds, Series 2019 (General Obligation - Limited Tax)

Credit strengths

- Strong institutional presence from Miami University which has provided consistent income tax receipts and a growing population base
- Very healthy financial operations with strong reserves

Credit challenges

- Income tax base concentration in the university, the area's largest employer, which may have a negative effect on the city's financial position should the university reduce operations.
- Above average unfunded pension burden arising from participation in two underfunded cost-sharing retirement plans.

Factors that could lead to an upgrade

- Strengthening of tax base via employer and taxpayer diversification.
- Maintenance of positive financial operations and strong reserves.

Factors that could lead to a downgrade

- Multi-year declines in fund balances and liquidity
- Deterioration of the city's tax base via loss of major employers
- Increased leverage from debt or pensions

Hope you found these Moody’s reviews informative and helpful. At first glance the General Fund ending balance looks like a large sum. The first chart points out that the General Funds projected ending balance is 58.77% of operating expenditures below the average of 68.17% over the 21 year time frame. Also directly related to this is the fact transfers out in the 2018 thru 2021 are declining also as less money is available for capital improvements and equipment purchases or discretionary spending options.

The second chart points out that operating expenditures are projected to be 90.78% of our operating revenue. The average over the 21 year time frame is 75.24% excluding the years 2008 thru 2010 due to ramping up of Fire & EMS services to a 24 hour operation and the Western Knolls settlement. This also excludes the lowest year 62.54% in 2001 and the highest year 90.78% in the 2021 budget. Again the more revenue that is dedicated to operating expenses the less you have available to transfer out for capital improvements and equipment purchases.

The third chart points out that we are expecting a $721,198 decrease in income tax receipts in 2021. The other two major drops in income are Hotel Tax receipts and Investment Income. As the COVID-19 pandemic eases and Miami starts to resume events and sports teams go back to a normal schedule, the Hotel Taxes receipts will increase but we will have one less operating hotel going further. If you listen to the Feds they project to keep their rates low well into the future which has a direct relationship on our Investment Income.

The fourth chart points out how between the General, Capital Improvement and Equipment Funds ending balances may change over time but we have less on hand in 2021 compared to 15 of the years over the 21 year time frame.

Two other expenditures to take into consideration is we have added the Wi-Fi annual payment and the possibility of continuing the Cold Shelter Transitional Housing pilot program we are paying for out of funds available in the 2020 cycle. These are large expenditures that will need continuing funding through the General Fund unless alternate sources of revenue become available. And finally hanging over our heads is the possibility of the State legislature not renewing the temporary allowance for the City to be able to receive withholding taxes for those individuals working at home as well as the lawsuit questioning the constitutionality of doing so.

In conclusion, my opinion is it is not prudent to fund anything out of our General Fund Balance at this time. We can plan, as we did with the municipal facilities improvements, to accumulate moneys for the future to fund these objectives. The only other alternative is reducing operating expenditures which are comprised of 64.29% salaries and benefits.

I hope you find this helpful in your decisions. It is a good practice to look at this issues at a higher level to help determine if there may be unintended consequences to a decision of this nature.