

## Budget Message

December 26, 2017

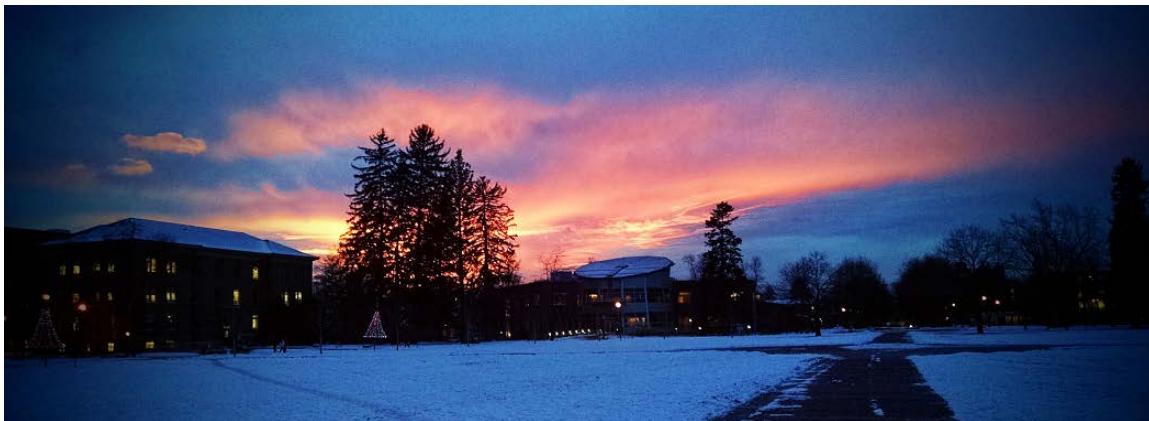
City of Missoula Residents:

This document is the Final Operating and Capital Budget for the City of Missoula, Montana for the fiscal year ending June 30, 2018 (FY 2018). A brief summary of the Final Budget follows.

### Overview of Budgeted Resources

The following table depicts the projected beginning balances, estimated revenues, final budgeted expenditures, and projected ending balances for the budget year. All city funds are included in this budget. The table reflects estimated revenues of \$158,479,877, budgeted expenditures of \$159,767,346 with anticipated expenditure savings of \$1,554,412, resulting in a projected increase in the overall ending balances of \$35,466,855. An explanation of the significant changes in fund and cash balances (those greater than 10%) are provided on the following pages.

Projected Changes in Fund Balances or Cash Balances Final Budget - July 1, 2017 through June 30, 2018 (FY 2018)								
	Governmental Fund Types				Proprietary Fund Types	Fiduciary Fund Types	Component Units	Total All Funds
	General & General Special	Special Revenue	Debt Service	Capital Project	Enterprise & Internal Service	Trust & Agency		
Projected Beginning								
Nonspendable/Assigned/Restricted	\$ 3,382,924	\$ 12,233,263	\$ 3,629,934	\$ 766,886	\$ 18,138,240	\$ 419,152	\$ 11,059,980	\$ 49,630,379
Unassigned	2,676,570	(1,195,469)	(379,471)	(9,663,970)	(3,159,213)	-	(1,154,502)	(12,876,055)
Total Fund Balance/Cash	6,059,494	11,037,794	3,250,463	(8,897,084)	14,979,027	419,152	9,905,478	36,754,324
Estimated Revenues	57,710,353	20,279,948	3,339,073	11,196,101	39,196,682	-	26,757,720	158,479,877
Approved Budget	(60,037,134)	(19,171,618)	(3,112,961)	(1,404,003)	(40,326,506)	-	(35,715,124)	(159,767,346)
Anticipated Savings	1,554,412	-	-	-	-	-	-	1,554,412
Projected Change in Fund Balance/Cash	(772,369)	1,108,330	226,112	9,792,098	(1,129,824)	-	(8,957,404)	266,943
Projected Ending								
Nonspendable/Assigned/Restricted	2,594,445	13,124,229	3,833,550	895,014	12,353,306	419,152	948,074	34,167,770
Unassigned	1,138,268	(978,105)	(356,975)	-	1,495,897	-	-	1,299,085
Total Projected Fund Balance	3,732,713	12,146,124	3,476,575	895,014	13,849,203	419,152	948,074	35,466,855



Listed below are explanations of the significant changes in fund balance/cash, for each of the major fund groups. The information below utilizes draft annual audit figures which were not available at the time of budget adoption. The fund balances in this discussion will differ from the "Projected Beginning Fund Balances" used throughout this document. The City of Missoula feels it is important to include more recently available information in this section of the budget document.

#### **General Fund (Major Fund) and General - Special Purpose Funds**

- The General Fund: The combined General Fund and General Fund Special Funds year-end fund balances decreased from \$5.49 million in FY 2016 to \$ 3.84 million at the end of FY 2017. Approximately \$1,600,000 of the reduction in the fund balance is due to an accounting issue in which the Capital Lease proceeds were distributed to the General Fund, two Special Revenue funds and the Wastewater fund. Annually the City purchases capital equipment and vehicles which are reimbursed in the form of capital lease financing. This spreads the costs of the equipment over several years in order to keep vital equipment functional and in service to serve the citizens of Missoula. All expenditures were charged to the Capital Fund and when the proceeds were received, the funds were distributed to the funds that were assuming the debt service, creating a negative balance in the Capital Fund. The accumulated financing proceeds were transferred back into the Capital Fund, reversing the trend of an increasing negative fund balance. In addition to the transfer of the \$1,600,000 from the General Fund, approximately \$160,000 of the reduction in the fund balance is due to expenditures related to the Parks and Trail bond and the timing of the reimbursement revenues from the County. In light of the decrease in the fund balance due to the accounting correction for prior year's equipment financing, the City is requesting General Fund departments commit additional 1.12% in budgetary savings to cover the reduction in fund balance and budgeted revenues. During the budget process for FY 2018, the City continues to budget conservatively for anticipated revenues and in combination with committed expenditure savings will strive to build back fund balance in the General Fund.

#### **Special Revenue Funds**

- Special Revenue Fund balances are usually fully appropriated to be spent, even though certain funds are targeted to have substantial year end fund balances to handle the ongoing operating expense of their programs without developing a negative fund balance (i.e.: Street Lighting Assessments Fund, Cable Franchise Fee Fund, Building Inspection Fund, Special District funds). Most of the other special revenue funds are slated to fully spend the beginning fund balance; the balance exists because projects were not completed during the preceding fiscal year, or the project is still in the planning stages.

#### **Debt Service Funds**

- The Debt Service year end fund balance is budgeted to be spent for all general obligation debt. Any fund balance in the special improvement district (SID) debt service funds is not being spent. The City is required to maintain a reserve equal to 5% of all outstanding SID bonds. In addition, the SID debt service funds are expected to build in size until bonds are called (redeemed) early due to prepayments of the underlying assessments supporting these debt issues.

#### **Capital Project Funds**

- The Capital Projects year end fund balance for FY 2017 was negative. The nature of the Capital Project Fund in which the funds are expended for approved projects and then reimbursed by debt issuance indicates the fund will realize a perpetual negative fund balance. In FY 2017, the negative

fund balance was reduced by 53%. This reduction is due to a realized accounting error in which capital lease proceeds were distributed to the funds assuming the debt. The financing proceeds were transferred into the Capital Project fund to cover the capital expenditures for the annual core equipment and vehicle replacement. The remaining negative fund balance will continue to fluctuate as projects are expended year to year and when completed, the fund is reimbursed through the issuance of debt or assessments.

### **Enterprise/Internal Service Funds**

- The City of Missoula now currently has five Enterprise Funds: Civic Stadium; Water Utility; Wastewater Utility; Storm Water Utility and Aquatics.
  - FY 2018 will be the first full year operating the Water Utility. There are no proposed rate increases for the Water Utility at this time. The rates will remain at the last approved PSC rate schedule. Given that there is little to no historical data of running the utility as a governmental entity, the proposed revenues and expenditures are based on a pro forma supplied by experts in the water utility field. For the next five fiscal years, the net fund balance is proposed to increase while maintaining the current rate fee structure and expending capital improvements in the \$5 million annually range. The capital improvements project schedule will upgrade and rehabilitate the aging infrastructure with the goal to decrease the leakage rate. More details are provided in regards to the capital projects in the Capital Project section of the budget.
  - The Wastewater Utility rates are scheduled to increase on January 1, 2018 by 2.5% for the final increase of a planned three year phase-in of rate increases, (2016 – 2018). Since FY 2016, the sewer utility realized an increase in revenues by an average of 3.30% per year with a modest budgeted increase in revenues of 2.95%. In addition to the sewer use fees, the City acquired Garden City Compost, formerly EKO Compost, and FY 2018 is the first full year operating the compost division of the Wastewater Utility. Based on historic analysis of the business and maintaining the existing price structure for tipping fees and compost sales, there is anticipated revenue of \$1,077,000. This will cover the costs of acquisition, personnel, operating supplies and site upgrades to be compliant with Montana Department of Environmental Quality requirements.
  - The Storm Water Utility was created to meet increased regulatory compliance for storm water runoff into local waterways. The Municipal Separate Storm Sewer System (MS4) permit is a requirement of all municipal governments to decrease the amount of contaminants entering the waterways via runoff from municipal streets/infrastructure. There is no current proposal to change to the rate structure. The Storm Water Utility is in the process of analyzing the rate structure through a rate fee study. When the study is complete the results will be presented to City Council with any recommended changes. It is anticipated that this rate study will propose an increase over the current rates. Any increase in rates will cover the necessary expenditures to meet regulatory requirements including hiring maintenance staff and future capital improvement projects.
  - Aquatics is budgeted to maintain its fund balance. The Parks & Recreation staff are reviewing the rate structure in regards to increases operating and personnel expenses and a rate change is anticipated to occur during FY 2018. This would be the first rate increase since FY 2009. It is expected that any rate structure change will result in an annual increase in fund balance.
- The City's only Internal Service Fund, the City Health Insurance plan, had suffered from significant increases in usage and medical inflation during the past decade causing a volatile fund balance. In an attempt to have a positive growth in the fund balance, the City increased the contributions on both the employee and on behalf of the City. In addition to the increased contributions, the City provided additional funding as onetime transfers from the General Fund for FY 2012 – FY 2015 to assist in maintaining a positive fund balance. In FY 2015, there was a slight reduction in fund balance due to an abnormal increase of costs to the program. This was determined to be an increased cost from the implementation of the Affordable Care Act (ACA). Part of implementing the ACA is that it is mandatory to include prescriptions as part of the total claim deductibles and this was not recognized prior to the implementation of the ACA. Again in FY 2017, the City experienced a loss in fund balance by a modest \$180,000. This reduction was due to a larger than anticipated number of larger monetary claims that were above recent historical trends. As a result of this drop in fund balance, the administration recommended that the City's funding of the health plan be increased by an additional 5% (\$40.00) per employee beginning October 2017 in addition to the 3% increase in the prior fiscal year. The City is committed to maintaining a three month reserve in the health plan based on budgeted expenditures. The target fund balance for FY 2018, meeting the

reserve requirement, is \$1,400,000. In an effort to meet the reserve requirement and stay ahead of the trend of increasing health care costs, the city has increased employee contributions and budgeted for insurance claims expense at a level 5% over the actual claims paid by the City in FY 2017. With these increases, there is a conservative estimate to increase the fund balance by \$200,000 to get closer to meeting the reserve goal. The Employee Benefit Committee has also been focusing on identifying methods to cut costs within the health plan by utilizing the assistance of the plans third party administrator, Allegiance Benefit Plan Management.

### **Component Units**

The City of Missoula has four component units: Missoula Parking Commission (MPC), Missoula Redevelopment Agency (MRA), Business Improvement District (BID), and the Tourism Business Improvement District (TBID).

- The Parking Commission has an operating budget of \$2.1 million plus debt service requirements of \$0.7 million. It maintains a debt service reserve of \$0.5 million, for the bond issued for the construction of an additional parking garage in the downtown business district in the spring of 2014. FY 2017 saw the first full fiscal year of operations after the implementation of new parking meters. This was a \$1.6 million plus venture that replaced all of the antiquated single-space mechanical parking meters with new multi-space digital meters (LUKE) that accept credit cards. The implementation of the LUKE machines increased parking revenue by 19%. In FY 2018 the Parking Commission is working with community partners and businesses to increase the available public parking capacity. In partnership with the Missoula Redevelopment Agency, the Parking Commission will receive an additional parking garage that is being constructed as part of a student housing project. This will increase the number of parking spaces available by more than 100 spaces. The Parking Commission is in the process of implementing License Plate Recognition (LPR) software to be used by the Enforcement Officers and at the gates of the parking garages. The implementation of the LPR will increase enforcement and provide greater efficiency for monitoring the downtown parking.
- The Missoula Redevelopment Agency (MRA) was created by the City Council to encourage new development and redevelopment pursuant to the adopted Urban Renewal Plans. Preserving existing public investment, enhancing the tax base, generating employment, and stimulating private investment are the means MRA uses to reclaim urban renewal areas. The MRA encourages infill development, provides for the adaptive reuse of the built environment, and reclaims blighted properties. MRA is empowered by State law and local ordinance to respond aggressively and with flexibility to redevelopment problems and opportunities. Through these activities, MRA also provides alternatives to urban sprawl outside existing municipal service boundaries. Missoula has six active Urban Renewal Districts (URDs) that are currently being managed by MRA. All of the districts have a tax increment financing (TIF) funding mechanism authorized by State urban renewal law. MRA is also working with the newly created Department of Housing and Community Development to identify opportunities to increase affordable housing in the community. The Agency's revenues are derived primarily from Tax Increment Property Tax, State Personal Property Tax Reimbursements, State Entitlements, and Investment Earnings. Small amounts of revenue are received from other miscellaneous sources. The Agency's fiscal year 2016 revenues were \$546,587 higher than in fiscal year 2015.

URD II, located in the heart of Missoula, covers the approximate area starting north at Toole Avenue, extending south to South 3<sup>rd</sup> Street, and starting east at Walnut Avenue and running west until Garfield Avenue.

URD III runs along the Brooks Street corridor in southwest Missoula. The approximate area that URD III covers, starts in northeast Missoula at 14<sup>th</sup> Street and Bancroft Street and follows the Brooks Street corridor southwest extending to Reserve Street and 39<sup>th</sup> Street. Recently URD III extended the boundaries to include parcels that the Southgate Mall occupies, and an area along the western boundary between Reserve Street and Montana Rail Link's Bitterroot Branch Line. The boundary modification in URD III allows for consideration of TIF funds to be used in upgrading infrastructure and expanding street connectivity in the area.

MRA has initiated programs to build sidewalks in URD II and URD III where they do not exist or are deficient. Approximately 13.2 miles of sidewalks have already been constructed with the goal of completing the sidewalk network in both districts within the life of those districts. Over \$10 million has been spent improving neighborhoods through the installation of sidewalks, curbs, street trees and repaved streets since MRA initiated the complete sidewalk program.

After successfully completing major improvements to Brooks Street between Reserve Street and Dore Lane, MRA made a commitment with the owners of the Southgate Mall to improve the infrastructure around the mall and create a new connectivity running east to west on Mary Avenue. This Mary Avenue project is investing \$10 million in improving the traffic flow and infrastructure in the area around the mall and off Reserve Street.

Two smaller districts located in downtown Missoula adjacent to the Clark Fork River are: The Front Street URD which generally occupies the area south of Main Street to the river, and west of Madison Street to one block east of Orange Street, and The Riverfront Triangle URD which occupies the area south of Broadway to the river, and west of Orange Street to the MRL Bitterroot Branch Line. The Front Street URD has active projects in the district including updating infrastructure around the Stockman Bank and working with community partners to assist with a large student housing project

The Hellgate URD, which is located east of Madison Street between Interstate 90 and the Clark Fork River and the North Reserve – Scott Street URD, located between Reserve and Scott Streets north of the MRL railroad and south of Interstate 90.

In the North Reserve – Scott Street district MRA is assisting with infrastructure upgrades to the national headquarters for a regional home health corporation, and for a new residential neighborhood named Scott Street Village.

- The Downtown Business Improvement District (BID) was created through the efforts of the Missoula Downtown Association to address the challenges created by the termination of the Downtown Urban Renewal District (URD I) on June 30, 2005. Implementation of the district began in 2001 with the creation of a committee, followed by community education through local media campaigns and meetings with property and business owners in the district. Following educating the citizens was the creation of a comprehensive database of property owners in the district, and the petition process to create the district. The verification of the petition was finalized at the end of 2004. The BID was presented and approved by the City Council in April 2005. The BID now serves as an advocate for property and business owners in the district and address areas such as safety, cleanliness, appearance, marketing, business retention and recruitment. The district also advocates for public and private investment in buildings and infrastructure.
- The Tourism Business Improvement District (TBID) was created through the efforts of the Missoula Area Convention and Visitor's Bureau to aid tourism, promotion, and marketing within the District. The creation of the district also allows Hotels/Motels outside the City limits in the Missoula Urban area to participate in the Tourism Business Improvement District. The goal of the TBID is to increase four season revenues statewide through effective marketing and promotions. In order for the TBID to accomplish its goal of increasing four season revenues by focusing on high-value, low-impact visitors by working in partnership with the Missoula International Airport to bring key new service to Missoula. The TBID also works with the community to keep and strengthen our present air service by promoting Missoula and Montana and by offering incentives to air services in an attempt to increase the total air service into and out of Missoula. Destination Missoula and the TBID will focus on increasing overnight visitation to Missoula with an emphasis on the months of November through April. In an effort to increase overnight stays in Missoula the TBID/Destination Missoula will leverage marketing funds focusing on Missoula being a prime destination for annual business meetings and/or conventions, sports and sporting events, tour, group, and leisure travel.

## Planning Processes

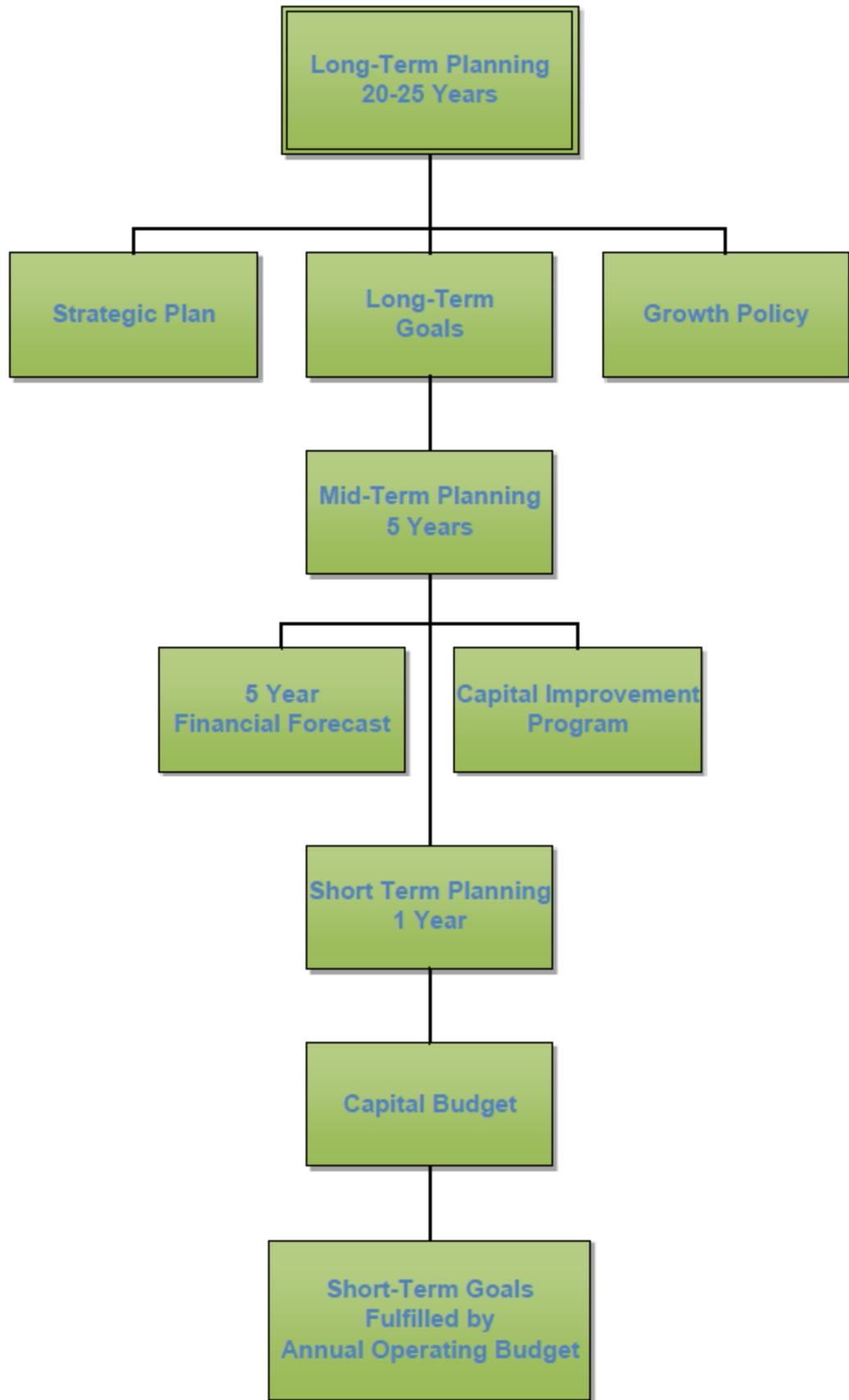


The City of Missoula conducts various planning processes (long-term, mid-term and short-term), to help guide the government and to ensure that decisions are made in the context of the organization as a whole and with a long-term

perspective. Diligent efforts are made to ensure each of these component planning processes are in concert with one another. This so called "Linkage" is paramount to insure short-term decisions are consistent with the overriding values embodied in the mid-term and long-term planning processes adopted by the City Council. This required linkage dictates that the Operating and Capital Budget be developed within the context of and consistent with, the City's long-term and mid-term plans.

Each element of the City's planning process has a different purpose and timeframe. The Strategic Plan, Vision, Mission, Long-term Goals and Growth Policy are the most far-reaching in nature — 20 to 25 years. The Capital Improvement Program and the Five-Year Financial Forecast are mid-term in nature — five years. The Annual Budget and the Capital Budget are short-term — covering a one year timeframe. The most important requisite is that they are coordinated efforts.

Shown below is a hierarchy of the City's layered planning processes, all which support one another and are designed with a common goal. The chart depicts how the Annual Operating Budget and the Capital Budget fit within the City's planning process hierarchy.





## Strategic Plan

Strategic planning suggests ways (strategies) to identify and to move toward desired future states. Strategic planning starts with the process of developing and then implementing plans to reach goals and objectives. Within government, strategic planning provides guidance for organizational management, similar to that for business, but also provides guidance for the evolution or modification of public policy and laws. Areas of such public policy include: funding of infrastructure and rate-setting, it also includes functional plans, such as the City's Growth Plan for land use, the City of Missoula transportation plan, the City of Missoula wastewater facility master plan, and City of Missoula fire master plan.

The FY 2018 budget continues our Strategic Planning initiatives started in FY 1992. This plan was significantly updated in FY 2009 and implemented in FY 2010 and updates continue through the current fiscal year. The City's Strategic Plan is an ongoing dynamic process that will provide residents, taxpayers and stakeholders a greater understanding of city government. The City's Strategic Plan focuses on performance and provides for measurable goals and objectives the City intends to achieve within the fiscal year. Department employees will be held accountable for the implementation and success of the plan. As part of the City's Strategic Planning Process, the city created a set of strategies to help guide the organization. These range from philosophical strategies down to concrete achievable goals for the coming year. The City's Strategic Planning Process, which is delineated into several charts and paragraphs, is listed below:

### City of Missoula Strategic Plan 2010-2018

#### Goal

**We believe the City of Missoula has a responsibility to remain financially stable and to provide service to its citizens.**

**We will work toward success in three areas:**

- 1. Fiscal Sustainability**
- 2. Harmonious natural and built environment**
- 3. Quality of life for all people in all places**



## City of Missoula Goals

The City created a set of short-term and long term goals and strategies. The short-term goals and strategies are those that guide the development of the budget for the coming year. Long-term goals and strategies are more far-reaching in nature and do not change from year to year, however are reviewed and updated every year.

Listed below are the City's Strategies that help guide the development of this budget. The goals and strategies listed below are addressed very specifically in each of the departmental narratives in this budget document. The extent to which a department can advance these goals and strategies is actually quantified and taken

into account when the individual offices are seeking funding for capital requests. Actual review, approval and funding for each of the capital requests is explained in the Capital Budget section of this report.

## City of Missoula Strategies

### Missoula will lead the region in the following three areas:

#### 1. Funding and Service

We will maintain or improve the level of service to citizens.  
We will work toward sustaining and diversifying fiscal resources.  
We will work with public and private sector partners in greater numbers to find new ways to enhance and diversify Missoula's economy.

#### 2. Harmonious Natural and Built Environment

We will make sure that our natural and built environments continue to represent Missoula's values of clean water and clear air.  
We will work to provide citizens access to parks, open spaces and the natural environment.  
We will reflect values of sustainability in transportation and building design.

#### 3. Quality of Life for All Citizens

We will work together to meet basic human needs with dignity for all.  
We will work to provide affordable housing for the work force of Missoula.  
We will support plans and programs that promote a healthy lifestyle for Missoula's citizens.

Departments develop and continue to develop performance measures to identify and track quantitative and qualitative measures of their service delivery performance. Performance budgets emphasize the accomplishment of program objectives. Performance budgeting involves a shift away from inputs (what is going to be purchased), to outcomes (what is going to be accomplished). Annually, the departments review their strategic goals and if the goals were met or need to be redefined. The departments revise the goals and strategies on an annual basis to ensure that they are short term, or can be accomplished within a year.

## Five-Year Financial Plan

Each year the City of Missoula evaluates its current financial condition within the context of existing programs, assesses future financial capacity, and integrates the City's Strategic goals, objectives, and financial policy into its decision-making process. Analysis of the City's financial and economic trends is an integral part of this process.

Finance Department staff perform financial trend analysis each year in conjunction with the annual mid-year budget analysis. This review utilizes budgetary and financial information to create a series of local government indicators to monitor changes in the City's financial condition. These indicators, when considered as a whole, can help interested stakeholders gain a better understanding of the City's overall financial condition. This type of analysis of key financial trends and other community factors is similar to the analysis that credit rating agencies undertake to determine the City of Missoula's bond rating.

Using this trend analysis and the framework of the financial policies adopted by City Council, management is able to strategically plan and budget, provide solutions to negative trends, and ultimately preserve the financial health of the City of Missoula. It is a good 'report card' of the City's current financial condition and reference point as staff begins work on the next year's budget. Most importantly, the financial trend analysis assists the City Council and the City administration in focusing on the "Big Picture" of the City's financial operations.

The City of Missoula is starting to show trends of increased building in both the commercial and residential portions of the city. This increase in the building industry is positive for the City due to the fact that at this time the majority of the City's revenues are dependent on the tax base. Since FY 2008, the start of the recession, the City was having difficulty raising revenues related to the stagnant growth in the building industry and many commercial businesses lay empty or for sale. During the recession, the goal of the City was to maintain a positive fund balance or increase the fund balance to the goal of a 7% reserve of operating expenditures. This is one of the major long term goals of the City General Fund. With the onset of increased spending in the building industry, the City has started to realize a small portion of the additional tax base, which translates into increased revenues from property taxes. Growth in the City is evident by the continued positive increase in the market value, which is discussed further in the budgetary trends section below. Although there is continued and steady growth, the City's revenues are still limited and reliant on taxes and the ability to tax the citizens within State statutes. The additional revenue generated from growth continues to be limited by the State Legislature which is restraining the growth factor by half a percent, as compared to three percent the growth factor prior to 2008.

For the future the City is looking into expanding services and space. Currently the City is experiencing overcrowding issues with the current facilities that house the staff and with the services provided. As the population continues to increase, there are greater needs in the services provided to the public. Every year, new FTE's and programs are being added which requires more overall staff. The current property that houses the police and internal services departments are constrained by space, with no room for expansion. As the number of FTE's and services continue to climb due to increases in services required by either need, statute, legal authority, or mandated requirements, the City is looking into acquiring additional property in order to consolidate staffing. Currently the City is renting space for three different departments and a number of staff members. Within five years, the municipal court may need to expand to add another courtroom and add additional staff for the possibility of a newly elected Judge. Since a majority of revenues are reliant on the tax base and the will of the State Legislature, the City has been actively looking into different revenue streams to supplement the anemic tax allowances. There has been discussion of creating a local option sales tax in an effort to diversify revenues to support City services. Another area of concern is the aging infrastructure and the funding for the infrastructure. The state allowance for the Gas tax has recently increased which will provide for some additional infrastructure funding.

## Capital Improvement Plan



The City prepares a five-year Capital Improvement Program (CIP) which is summarized within the Annual Operating Budget. The CIP is a multi-year capital improvement plan that forecasts, but does not obligate, future spending for all anticipated capital projects. The CIP is developed and updated annually. The proposed five-year CIP uses conservative financial forecasts and reflects only those projects with the highest priority, that are mandated by the law or some other legal obligation and projects that have the most realistic expectation for completion during the next five years.

As in recent years, the City continues to face numerous capital funding requests. At the same time, the City has finite resources and limited taxing authority to fund the operating costs for many of the proposed capital projects. The proposed five-year CIP attempts to continue, and even expedite, priority projects and projects that are legally obligated, while ensuring long-term sustainability for operating impacts.

The Annual Budget Process includes a re-evaluation of the capital projects included in the CIP for the coming year as well as the anticipated funding sources for the projects. If

approved in the Annual Budget Process, the capital items appear in the Annual Operating Budget, which constitutes the formal spending authority for the project. The capital items included in the Annual Operating Budget represent the "Capital Budget".

The City of Missoula utilizes capital lease financing to purchase vehicles and equipment that have outlived their useful life and have been determined by the vehicle maintenance manager to be in need of being replaced. Each fall the City enters into a new capital lease agreement from the vehicles and equipment purchased the prior year. The goal of the City is to enter into a capital lease agreement that total around \$1.5 - \$2.5 million per year with a future lease payment averaging about \$475,000 per year. With the City entering into a lease agreement every year and existing lease payments expire, this maintains a consistent debt payment of approximately \$1.5 million per year. This is the amount used for future capital lease payments when developing the budget and in determining the vehicle and equipment replacement schedule.

An additional summary of the significant capital projects included in the FY 2018 Operating Budget is included in the Capital Projects Section of this budget. The Capital Projects Section includes the details of the current and estimated future debt payments based on the vehicle and equipment replacements schedule.

## STAFFING CHANGES

The final budget includes a net overall increase of 54.24 full-time equivalent employees (FTE). The chart below shows the change in FTE for the budget year for each department. Also, included in the appendix is a chart that shows the City's FTE over the last five years.

<b>Staffing Changes (FTE)</b>	
<b>DEPARTMENT/DIVISION</b>	<b>Net Increase (Decrease)</b>
<b><u>General Fund Departments</u></b>	
Human Resources	1.00
Municipal Court	(1.50)
Finance/Treasurer	(1.00)
Central Services	(1.00)
Facility Maintenance	2.00
Development Services	1.73
Housing & Community Development	2.00
City Attorney	1.00
Street Division	(1.50)
Fleet Maintenance	(1.30)
Police Department	(0.01)
Parks and Recreation	(0.02)
<b>Total General</b>	<b>1.40</b>
<b><u>General Fund Special &amp; Special Revenue Funds</u></b>	
Fort Missoula Regional Park	5.71
Planning	1.00
Building Division	1.52
Road District 1	1.72
Parks District 1	1.27
Transportation	0.10
<b>Total General Fund - Special &amp; Special Revenue</b>	<b>11.32</b>
<b><u>Enterprise &amp; Component Unit Funds</u></b>	
Aquatics	0.36
Wastewater	6.16
Water	32.00
Storm Water	2.00
Parking Commission	1.00
<b>Total Enterprise &amp; Comp Unit</b>	<b>41.52</b>
<b>Total for City</b>	<b>54.24</b>

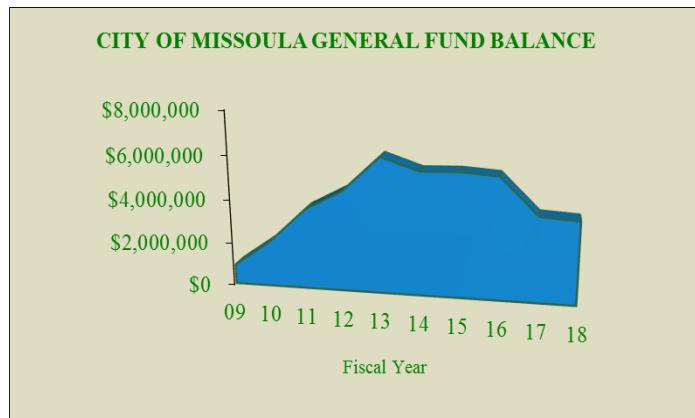
In FY 2018, the increase to the number of FTE appears to be a large increase, when in fact, the actual increase is 6.37 FTE's. The remaining 47.87 FTE's are due to the creation of new departments and/or newly acquired utilities. The largest increase is from the acquisition of the water utility. The other large increase is from the purchase of the compost facility, which added 6.16 FTE. The remaining increases are from the completion of the Fort Missoula Regional Park, creation of the storm water utility and creation of the Housing and Community Development department.

## BUDGETARY TRENDS

Shown below are a series of key financial indicators and budgetary trends that affect the ability of the City to sustain current service levels, while maintaining financial stability.

Fund balance measures the net financial resources available to finance expenditures of future periods.

Rating agencies examine fund balance when considering the credit quality of the City.

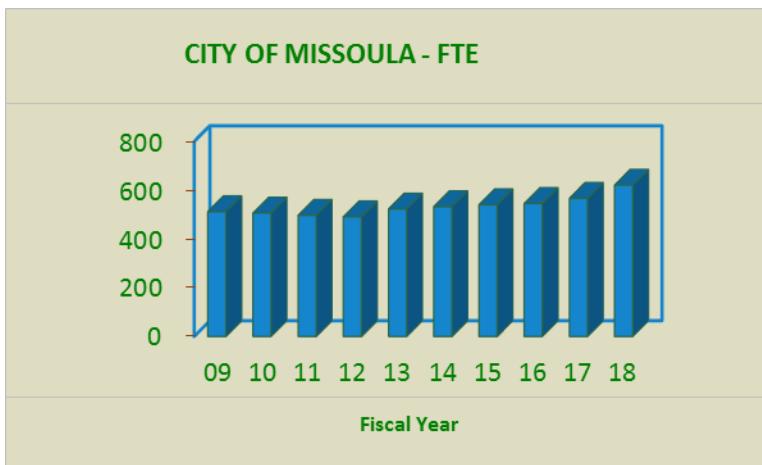


The General Fund balance is one of the better indicators of the City's overall financial health. Shown by the graph to the left is the City's actual General Fund balance over the course of the last ten years. Although not shown on the graph, the reduction in General Fund balance from FY 2001 to 2003 was attributable to several factors including the financial losses associated with a Fire arbitration settlement and a business licensing lawsuit as well as the transfer of nearly \$1,000,000 to stabilize the City's Health Plan and set up the City's Building Inspection Division as a separate fund. Subsequent to FY 2003,

the City has made a conscious effort to rebuild the General Fund balance. At the end of FY 2008, the total fund balance of the General Fund was \$1.2 million compared to \$1.0 million at year end in FY 2003. The decrease in fund balance in FY 2008 was due to a decline in expected expenditure savings and slight increase in tax delinquencies. An item of note is a historic review over the past 15 years indicates the City has consistently have between 3% - 5% in expenditure savings. The City addressed this issue by requiring mandatory holdbacks on expenditures ranging from 0.5% - 3.7% starting in FY 2009 and continues through the current fiscal year. The FY 2008 expenditure savings were less than 1% due to the heavy operating impact of higher fuel, energy and transportation costs that became imbedded in virtually everything the City purchased. The decrease in fund balance in FY 2009 was primarily due to a decline in expected revenues, especially in the fee based services related to the decline in economic expansion (planning and engineering fees, business licenses), investment earnings and in police fines. The decrease in collections on fee based services resulted in a decrease in the General fund balance from \$1.2 million to \$0.9 million.

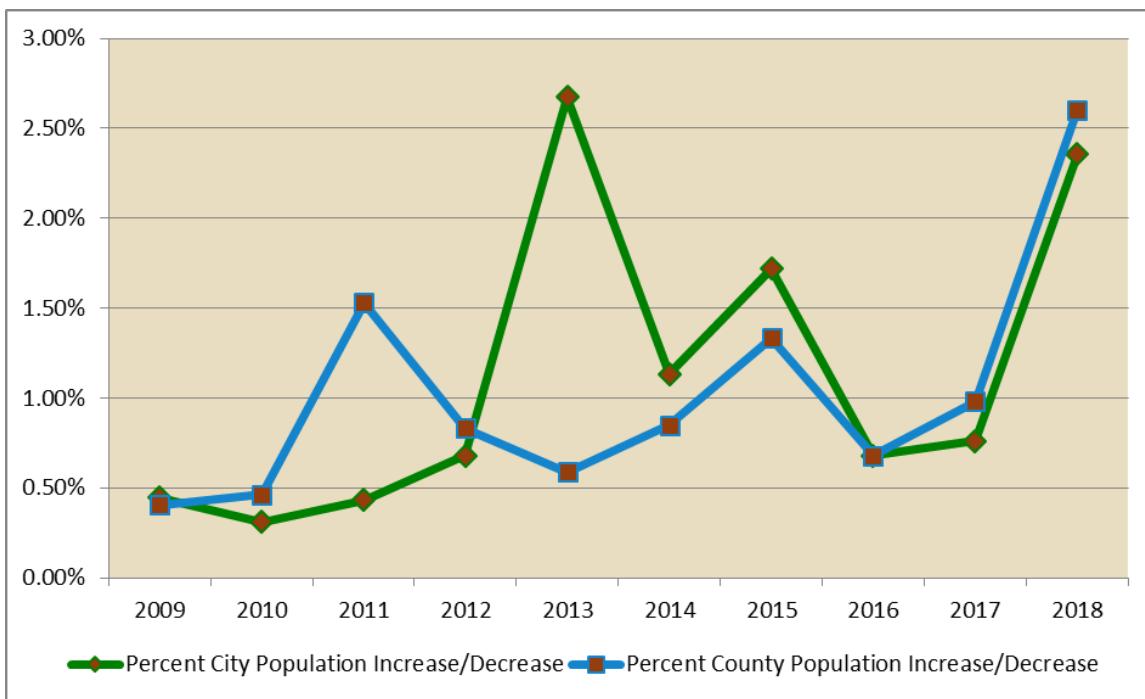
In order to combat the reductions in the general fund balance, the City's budgets continue to be structurally balanced, permitting the City to increase its General Fund year-end fund balance from \$0.9 million in FY 2009 to the high point of \$6.14 million by the end of FY 2013, meeting the 7% fund balance target. However, the fund balance continues to show a decline through the year end FY 2016. The continued building of the fund balance from FY 2009 through FY 2013 was accomplished by budgeting conservatively for revenues and by mandating significant expenditure savings from many large General Fund departments. Please note that seven special purpose funds under General Fund control were removed from the Special Revenue fund category at the end of FY 2010 and moved to special purpose General Fund accounts in FY 2011, causing an increase in the assigned fund balance by \$1.5 million.

Using the draft audit financials references in the changes to fund balance discussion beginning on page A-9, we are able to project fund balance in the General and General Fund Special Purpose Funds for FY 2018 at an estimated \$3.8 million with an estimated ending fund balance of \$3,732,713. The reduction in fund balance can be attributed to the assigned fund balance in the special purpose General Fund Accounts. This is to be expected, as the funds in these special purpose accounts are set aside for special projects and/or improvements. Even though the overall general fund balances are expected to reduce, the City intends to rebuild the FY 2018 unassigned General fund balance by over \$600,000 in FY18 in order to build the fund balance up towards the targeted 7%. The unassigned fund balance target is 7% of operating expenses. This percentage was identified by the City and the City's rating agency as an adequate target level for the unassigned fund balance in the General Fund.

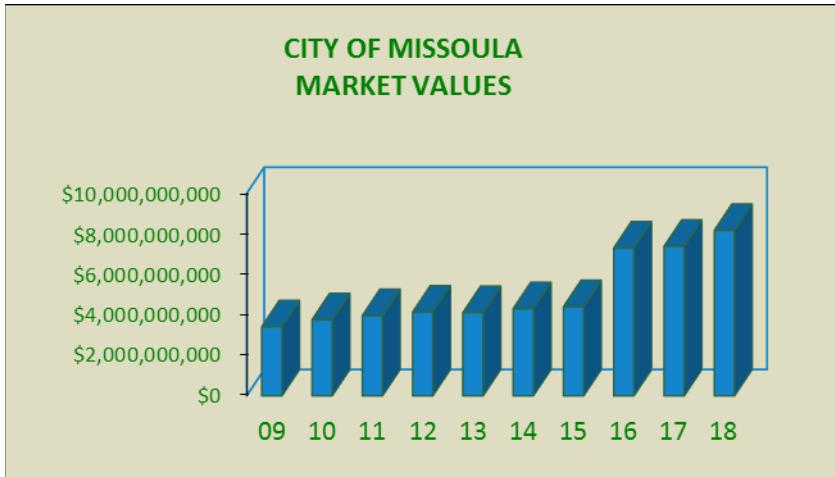


Full-time equivalent employees (FTE) are a key indicator mirroring the growth of the City of Missoula. As shown by the graph on the left, total FTE's grew to 512.17, and then reduced back to 491.29 by FY 2012 in reaction to the recession. Due to the fact that revenues had stabilized and have been increasing for several years successively, and related workloads have also increased due to the uptick in the building industry activity, the City has decided to increase the number of FTE's by 14.44% (81.85 FTE's) in all departments since

FY 2012. An 11.18% (46.57) increase in FTE's in the General Fund and a 1287% (12.87) increase in FTE's in Road and Park District 1 funds which are primarily supported by non-tax revenues. These were the first increases in a number of years, which equates to a 14.27% (59.44 FTE) increase over this 10-year period, while the City's population is estimated to have increased 0.91% during this same period of time. Please note that 23 of the new FTE's in FY 2013 were transferred to the City from the County Planning Offices (along with their own funding streams). If these FTE's were backed out of this calculation, (as they are predominantly self-supporting), the actual growth of new FTE's would be 5.32% compared to the population increase of 0.91% over the last 10 years. Not included in the calculations is the addition of the water utility, compost and storm water utility. The increases attributable to the utilities is an overall increase by 42.16 FTE's, which translates into an additional 7.44% of FTE's from FY 2017.



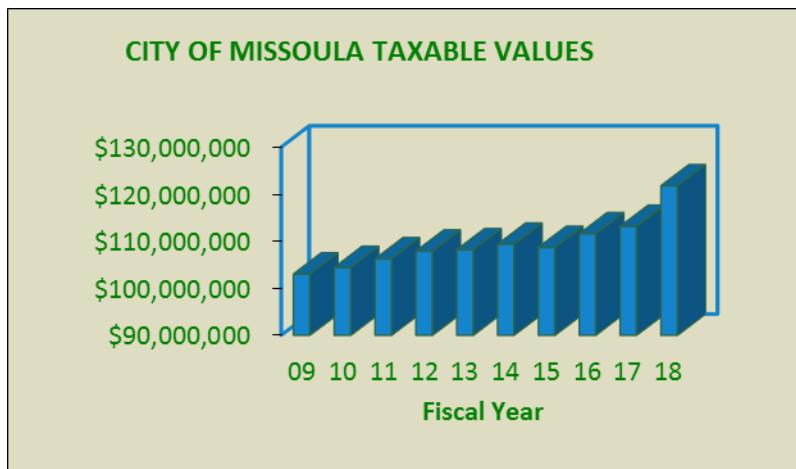
One of the principal challenges continually facing the City is the on-going financial obligation of new employees necessary to meet the service demand that accompanies the growth of the City. All indications are that the growth Missoula has experienced in the past will continue for the foreseeable future.



As a general rule, all real and personal property in the State of Montana is subject to taxation by the State. In addition to taxation by the State, its counties, municipalities and other political subdivisions have the ability to levy taxes. This rule is subject to exceptions in the case of specified classes of exempt property. Property is classified according to its use and character. The different classes of property are

taxed proportionately based on their market valuation. Property valuations are based on comprehensive appraisals of all taxable property and is performed by the Department of Revenue each year. The Department of Revenue certifies market and taxable values to each city on or before the 1<sup>st</sup> Monday in August. The trend of the City of Missoula's market value is shown by the graph above. As reflected by the graph, the City's market value has increased from \$3.412 billion in FY 2009 to \$8.176 billion in FY 2018, for a 141.38% increase over this period. The market value of property in the City reflects the rapid growth the City is experiencing. The graph of taxable values that follows reflects the City's ability to raise general tax revenue necessary to support the growing demand for government services.

The taxable value for property is determined by applying a statutorily established percentage ratio to the market value of the property, according to its property classification. The applicable ratio for most commercial and residential real properties is currently approximately 2.6%. Shown on the right is a history of the City's actual taxable value since 2009. The increase in taxable values does not coincide with the increase in market values because of



adjustments to the percentage ratio by the Montana Legislature and by changes in tax policy implemented through property tax amendments. The adjustments by the Legislature were designed to prevent local taxes from increasing at the same rate as property values. The taxable values (as opposed to market values) more accurately reflect the ability of the City to increase tax revenues. As illustrated in the graph, the City's taxable value increased from \$103.008 million to \$121.756 million from 2009 to 2018, an increase of only 18.54%, which is well less than a quarter of the increase in the market value of the same property. In recent years, the State has been placing a large restriction on the percentage of newly taxable values as compared to years past. As indicated in FY 2009 the taxable value was \$103,008 and in the current year the taxable value is \$121,756, an increase of \$18,000. In FY 2009 the inflation factor provided by the State was 1.672% and this resulted in an additional \$245,847 in revenue. Compared to the current year, the State restricted inflation rate is 0.590%, which resulted in an increase in revenues of \$278,840. With the restrictions on the ability to leverage annual growth from the State, it has made it difficult to fund projects and new requests that are sorely needed, without finding other avenues of revenue.

## SHORT TERM INITIATIVES – MAJOR ISSUES & SOLUTIONS

1. The FY 2018 budget, as adopted, was brought to Council in mid-June, earlier than the previous year, and in line with the accelerated schedule adopted in FY 2013 to approve the next fiscal year budget prior to the end of the current fiscal year. The calculated additional property tax impact for the current fiscal year is a reduction of 1.19% for City taxes and City-wide Road and Park District assessments, which is estimated to be a reduction by approximately \$26.40 per year for a home with a market value of \$250,000.
2. The FY 2017 budget includes 2.75% increases for Planning, Fire, Special Events, Business Licenses and Development Services. Building Inspection fees are being held at the current level for this year with the proposal of decreasing or adjusting the fees. The 2% increases in these areas as of service will not take effect until January 1, 2018. Several years ago, the City chose not to increase any charges for services fees. At that time, the decision to not increase the fees had a negative effect on the fund balance, as it declined due to increased administrative costs associated with operating these programs. The fund balance took the hit since there was not additional revenue to cover the administrative cost increases that occurred during the year. This year (FY 2018) as well as in the past four years (FY 2013 – FY 2017), based off the experience in FY 2011, and the continuation of annual cost increases for administering the programs, administration has determined that fees should increase by 2-3% each year in the Business Licensing, Development Services and Planning areas.
3. The actual level of new tax revenue from growth in the City's tax base for the current fiscal year (FY2017) is \$429,000. This compares to growth in past five fiscal years of \$452,529 for FY 2016; \$195,197 for FY 2015; \$299,612 for FY 2014 and \$271,813 for FY 2013. The City has budgeted for inflationary trending of property taxes allowed by state law (\$124,594).
4. City property taxes were not raised to support the increased expenses of the General Fund and in the city-wide assessments supporting expanded service in the Special Road and Park Districts. General Fund increases also relate to the City continuing to honor its union contracts. During the heart of the recession (FY 2008 – FY 2011) the City cut overall expenditures by 11% and reduced the workforce by 22 FTE's. Aside from the proposed salary increases for union and non-union staff in during that time and through FY 2017, virtually no new tax funded requests were proposed or approved due to the limited growth in taxes, except for several mandatory expenses such as costs associated with elections that occur in alternating budget years and the mandated Department of Justice agreement related to handling cases that involve rape. Starting in FY 2018, administration and Council met and determined strategic initiatives for the FY 2018 budget that identified the priorities of the administration and Council. These initiatives focused on public safety, supporting existing programs and projects and infrastructure. This is evidenced by the approved new requests that will be outlined further in the budget document. On the expenditure side, the largest expense is wages and benefits. Roughly 78% of the General Fund budget is devoted to personnel costs. For FY 2018 there is an increase in FTE's by 54.24 of which over half is due to expansion of services such as adding the Water Utility, Storm Water Utility, Compost and creation of the Housing and Community Development Department.
  - Property taxes were maintained for support of the City's Health Plan, as the plan has performed better in the last two fiscal years even though the fund took a hit in FY 2017. Prior to FY 2010, the City's Health Plan had consistently built fund balance for six consecutive years, and had \$2.3 million in surplus at the beginning of FY 2010. From the period of FY 2011 – FY 2015 the fund was very volatile and difficult to predict. During that time, the General Fund injected several large amounts of funds in order to stabilize the fund. One of the ways the City has leveled out the volatile nature is that for the past two year, the contributions on behalf of the employees has increase by 3% and then an additional 5% in FY 2018. With the additional increases in contributions and increased proposed expenditures, the proposed ending balance for FY 2018 is expected to grow by \$200,000 The City has also been focused on identifying ways to cut costs within the Health Plan utilizing the assistance of the plan's third party administrator, Allegiance.
5. Assessments were increased in the newly created Road Special Maintenance District, as the City attempts to increase the level of service delivery in this core area of service. Special Districts (Missoula has Road and Park Districts) are in place throughout Montana. Per the request of the City Council, the FY 2015 budget included a significant Road Special District funding increase of \$200,000 associated with additional annual support for the startup of a sidewalk support program that was initiated in FY 2014 with the goal to increase the amount of sidewalk projects initiated in the upcoming years. The FY 2018 commitment is \$370,000 of City support. The increased Special Road District assessments is identified as adding 1.72 FTE. This increases the number of FTE for the Streets Department to use for crack-sealing activities and snow plowing in the winter. The Park District assessments are used to support conservation lands, routine maintenance parks, median-greenway

maintenance, urban forestry, spray decks, and maintenance and operational support of the new Fort Missoula Regional Park that opened in the fall of FY 2017 and the County portion of Phase II to open in the spring of 2018

6. Standard & Poor's and Moody's, our ratings agencies, recently completed an updated review of many of our City credits. All of the City's credits were re-affirmed and sustained, which is a very positive factor while two credit ratings were increased by Standard and Poor's:
  - a. The City's GO Bond rating was increased from AA- to AA+
  - b. The City's General Fund Obligation Bonds from A+ to AA

One of the areas of concern in prior reviews was that a number of revenue streams that support General Fund functions had been allowed to accumulate balances outside of the General Fund and, to some extent, outside of the City's direct oversight. Many of these funds are now accounted for within General Fund during this budget process and will be kept under administration review and oversight going forward. The purpose and intent will not change for these revenue streams, but they will no longer be allowed to accumulate outside of the General Fund and will be managed more closely by the administration in the future. Standard & Poor's also recommended that future budgets plan to increase the General Fund year-end unassigned fund balance to 7% of the General Fund expenditures per the City's adopted financial policy. Every fiscal year since 2013, the City has budgeted to increase the fund balance in the General Fund.



7. Funding anticipated from HB124 (city entitlement from the State of Montana) is projected at \$8,552,718 for FY 2018, an expected increase of \$389,913 over FY 2017. State legislation reduced the entitlement share pool for FY 2016 to "Appropriate emergency money for new or expanded mental health crisis intervention" per HB33. The entitlement is back to normal funding starting in FY 2017.
8. The Building Inspection Fund is fully recovered as economic conditions continue to improve in the construction portion of the Missoula economy. The Building Inspection Division had previously reduced the staffing by four positions several years ago, Facility and Vehicle Maintenance has taken on the responsibility of maintaining and determining the replacement schedule and costs for the inspector's vehicles and there was a recent upgrade to the permitting system software, a cost that has generated many benefits to both the building community and City staff. The Building Inspection Division has been able to maintain its staff since there was an increase in its staffing by 1 FTE in FY 2016.
9. Impact fees are budgeted conservatively and are anticipated to generate approximately \$1,800,000 of revenue for FY 2018, over \$1.88 million were received in FY 2017 illustrating the uptick in construction seen across the city.
10. The City is permitted to levy what is necessary to fund voter-approved General Obligation (GO) Bond debt service. In FY 2017, the City will drop the levy to cover the bond payments (9.35 mills in FY 2018 from 14.02 in FY 2017).
11. General Fund support for the City's Capital Improvement Program will be of \$1,401,503 for FY 2018, compared to \$1,330,841 in FY 2017. In FY 2018, CIP support includes the required General Fund fixed payments plus the scheduled General Fund vehicle and equipment replacements. In addition to the vehicles and equipment, some of the notable projects are the completion of the Police Evidence and Storage building, continued IT infrastructure upgrades, phase II of the Wayfinding project and several parks around the City. The City Administration, in conjunction with all City offices, has developed a long-term (20-year) equipment replacement schedule that addresses the fact that the equipment replacement needs are more than \$2 million greater in the first five years (FY 2009-2014) than in the following five years. Six years ago, the City proposed to smooth out this wave of deferred equipment replacement by financing the equipment scheduled for replacement over successively shorter time frames in the future. This allows equipment to provide better service to residents during fiscally constrained times such as these. There are many Non-General Fund CIP projects that were not affected by the extremely tight funding in the General Fund these past years.

12. The General Fund baseline budget appears to be adequate for the new fiscal year for both fuel and energy costs. The City adopted the Conservation & Climate Action plan which outlines a strategic path to an overall goal of carbon neutrality for municipal operations by 2025. The strategies are organized into three main focus areas of operations: Fleet and Facilities, Internal Policies and Practices and Renewable Energy and offsets. Strategies to meet the goals of the Conservation and Climate Action plan include adding GPS units to the rolling fleet to improve efficiency and reduce fuel consumptions/costs. The City is in the infant stages of the All-In-One recycling pilot, which involves, City Hall, Council Chambers, Street Division and Facility and Vehicle Maintenance. Another strategy is performing a solar study to gather information about installing solar cells to City facilities to reduce the dependence on purchasing electricity from vendors. Central Services is conducting a baseline zero waste study in conjunction with Republic Services in an effort to decrease the amount of refuse the City disposes of every year.
13. This General Fund budget includes cost of living increases of approximately 2.75% for non-union staff. All union contracts were negotiated and approved in FY 2016. On average, there is a negotiated 2.75-3% raise to union staff.
14. Inflation based on price indexes for postage (proposed increase in first class stamps by 4.25%) and a 6% increase in electricity based on an approved rate increase for Northwestern Energy by the PSC. Assumptions for operating supplies or purchased services were accepted into the budget, unless a pre-existing contract for service allowed for a scheduled increase in FY 2018.
15. The program enhancements allowed in the FY 2018 budget are detailed in the appendix.
16. The economic factors driving the budget development are discussed below in the next section of the budget message.

## **ECONOMIC FACTORS**

- University of Montana economist, Patrick Barkey, has forecast that Montana's economic growth will be around the 3.2% range, which continues an improvement that began in 2014. Patrick Barkey has also projected that the Montana economy will outperform the national economy this next year.
- Missoula continues to see growth in the construction and manufacturing areas of the economy and in the financial and business industries. There are four identified areas that are proposed to see growth in the upcoming year: UM and State Government; Healthcare; Professional Services and Manufacturing of wood products. Due to an increase in these industries, Missoula is starting to realize a positive and favorable growth.
- The Missoula Economic Partnership, a public-private economic development organization, opened its doors in June 2011 and is fielding calls from a variety of fronts for business relocation, granting activity, expansion assistance and more. Since the Partnership has opened its doors, the Missoula employment market has enjoyed an increase of 750 jobs. These jobs center around basic industries, such as computer based technologies, manufacturing and health services.
- All of these factors were considered in preparing the City of Missoula's budget for the 2018 fiscal year. The decline in revenues in FY 2009 through FY 2012, especially in the fee based services related to the decline in economic expansion (planning and engineering fees, business licenses) has reversed and these revenues have been increasing each year since FY 2012.
- Sewer utility rates were increased modestly (2.5% per year) for the past three years beginning in FY 2016 to fund capital improvement projects. This takes into account increasing the capacity of sanitary sewer pipelines and pump stations to accommodate the growth and residential construction that is being planned for in the Linda Vista and Miller Creek areas. The City has continued to grow in population and in new sewer connections at a rate of approximately 1.5% per year. The sewer fund has been able to continue to build the fund balance to accommodate future projects, however the growth for the past couple of years is not adequate to cover the necessary and requested upgrades to the sewer treatment plant and sewer infrastructure therefore the modest increase in rates by 2.5%. In FY 2017, the City completed the purchase of EKO compost, renaming it to Garden City compost.



## **Closing**

We hope the information contained in the FY 2018 Final Budget is of benefit to all interested parties. In closing we want to tell the public that we made dramatic changes in the budget process starting in FY 2008 that continued through the current budget process. We have been actively pursuing a Performance Based Budget process since FY 2008. We strongly encourage each and every person using city services to inform us of their ideas, level of satisfaction and problems.

Respectfully,

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John Engen, Mayor