ERIE COUNTY FISCAL STABILITY AUTHORITY ANALYSIS OF THE ERIE COUNTY 2018-2021 PROPOSED BUDGET BASED FINANCIAL PLAN

October 24, 2017

1. INTRODUCTION

This report details the analysis and comments of the Erie County Fiscal Stability Authority (ECFSA) in its review of Erie County's 2018 proposed budget and associated financial plan. The ECFSA is charged with reviewing the county's submission in light of opining on reasonableness and do-ability. Under the legislation that created the Authority, within 20 days of receiving the county's submission, the ECFSA is required to determine, in its best judgment, whether the budget and plan are in balance.

In its current version of the plan, the county is facing $475,000 in fiscal gaps prior to any adjustments to the county's estimate. This gap is $7.44 million lower than the plan based on the 2017 adopted budget. The 2018 recommended budget property tax levy results in a $14.9 million increase in the county's tax levy, as compared to the 2017 adopted budget – a 6.01% increase. The county has provided evidence that the levy does not exceed the property tax cap and that the tax rate per thousand of valuation decreases by $0.01, from $4.95 to 4.94.

2. MAJOR PLAN ASSUMPTIONS

Major assumptions in the financial plan include:

1. 2018 sales tax growth of 2.6% over the county's 2017 adopted budget (1.75% over expected Y/E 2017 receipts), then 1.75% for 2019, and 1.5% for 2020 and 2021.

2. Real Estate Market Value Growth, impacting the county's property tax levy, is assumed to increase by 5.91% for 2018 and by 2.75% for 2019, 2.25% for 2020 and 1.5% for 2021.

3. The county portion of the property tax levy increased by $14.9 million in 2018. Then increases by $7.23 million in 2019, $6.08 million in 2020 and $4.14 million in 2021 – a total increase of $32.36 million over the period of the plan.

4. The county has not budgeted the full amount of ECC related chargebacks as a revenue in its budget. It has budgeted $3.6 million, approximately half of the anticipated chargeback revenue amount.

5. The plan narrative lists increase in health insurance rates of 5.3% for 2019, followed by a 5% increase for 2020, and 6.5% for 2021. However, current employee health insurance spending is reduced by 1.14% as compared to the 2017 adopted budget and increases for 2019-2021 respectively are: 2.89%, 4.79% and 6.31%.

6. Personal services expenses increase for step and longevity increments, as well as current contractual cost of living increases agreed upon through collective bargaining. For the labor agreements that expire during the period of the plan there is no allowance for potential negotiated wage increases.

7. Overtime expense rises at a rate significantly higher than the anticipated increase in salaries – 19.37% for 2018 (as compared to the 2017 adopted budget), then 2.1% for 2019, 1.5%for 2020 and 3% for 2021.

8. Capital borrowing of $42.1 million for 2018 and between $38 and $40 million for 2019, 2020 and 2021.

9. The plan, as presented, shows no gap for 2018 and shortages of $272,000 for 2019, $104,000 for 2020 and $99,000 for 2021.

10. The budget and financial plan, to balance, assume $17 million in credits against ECMC related IGT and DSH expenses. Credits were generated through savings provided by an ECFSA borrowing for ECMC capital projects. Including a new, state-of-the-art emergency room.

3. MAJOR ADJUSTMENTS – 2017 ADOPTED BUDGET AND PLAN TO 2018 PROPOSED BUDGET AND PLAN

Major revenue and spending revisions from the version of the plan based on the 2017 adopted budget include:

- The Property Tax levy has increased by $22 million for the 2018-2020 period, as compared to the 2017 adopted based plan.

- Full time salaries are increased by $6.4 million for the period 2018-2020.

- Vacancy savings for the period of the plan have increased by $700,000 for the 2018-2020 period. An additional $1.1 million has been included in the 2021 fiscal year forecast for vacancy savings.

- The 2018 proposed county budget has an additional 46 full-time positions in the general fund, as compared to the 2017 adopted budget. Other county funds include an additional 5 full-time positions. The total position increase across funds for 2018 totals 51 full-time jobs.

- Fringe benefit costs have decreased for the 2018-2020 period by $21.3 million as compared to the 2018 adopted budget version of the plan. The greatest change is in medical insurance costs. $14.5 million for current employees and $11 million for retirees.

- Fringe benefit rates over the period of the current plan increase slightly each year from 51.38% in 2018 to 54.52% of salaries in 2021 for current county employees.

	2018	**2019**	**2020**
2017 Adopted Plan	53.87%	54.43%	55.04%
Current Plan	51.38%	51.61%	53.04%
Increase	**2.49**	**2.81**	**2.01**

- County stated “gaps” are smaller in the most recent version of the plan as compared to the adopted 2017 plan. In that version, the shortages totaled approximately $7.9 million. The current plan calls for shortages of $475,000.

- The 2018 fiscal year assumes the use of $6,000,000 in fund balance as revenue to balance the budget. In addition, there is a special fund balance usage of $4.26 million, related to ECMC borrowing savings. The previous version of the plan called for $6 million in fund balance usage for each of the 2018-2020 years. The current plan assumes that $6 million amount, plus $4.26 million in special fund balance usage for the 2018-2021 period, totaling $17 million.

- Certain Health and Human services program costs have been assumed to be significantly reduced, over the 2018-2020 period, as compared to forecasts in the 2017 adopted budget based plan:

    - Family Assistance - $5.8 million
    - CWS Foster Care - $2.7 million
    - Safety Net Assistance - $2.4 million
    - Child Care DSS - $15.7 million
    - Children with Special Needs - $2.8 million

4. PLAN ASSESSMENT

The stated gaps in the current financial plan are lower, as compared to the previous version that was accepted by the Erie County Fiscal Stability Authority. In the current version of the plan (as compared to the previous version), sales tax revenues have been increased, health insurance estimates have been reduced, certain health and human services program costs have been reduced and $17 million in ECMC related ECFSA borrowing credits have been added as a revenue. With these items, the 2018 budget and associated 2018-2021 financial plan appear to be reasonable and achievable.

The following is a comparison of current and 2017 adopted plan annual gaps (in millions of $'s):

	2018	***2019***	***2020***
Current Plan Gap	***$0.27***	***$0.10***	***$ 0.10***
2017 Adopted Plan Gap	***$2.22***	***$4.77***	***$ 0.91***
Difference	***($1.95)***	***($4.67)***	***($0.81)***

Baseline Estimates/Associated Risk

1. ***Erie County Medical Center Corporation (ECMCC) IGT, DSH and UPL*** –In the previous version of the financial plan, the county appropriately added $60 million as a liability to be paid out over a four-year period. At the time, the county had a concept for a credits/points system that could be used to reduce that outlay. The ECFSA, upon closing its borrowing on behalf of the Medical Center generated significant savings resulting from its higher bond rating. A calculation, agreed upon by County and ECMC officials, determined that $17 million in points/credits generated by ECFSA savings could be used for county payments related to ECMC. $12.78 million of those funds is being used by the county for each of the four years of the plan, to help balance its budget.

   However, given ECMC's contractual relationship with the county, federal changes to the Affordable Care Act and/or Medicaid reimbursements may impact county finances going forward.

2. ***Sales Tax Revenues*** – The plan assumes a 2.6% increase in 2018 sales tax revenues over the 2017 adopted budget, and 1.75% over anticipated 2017 receipts. That is followed by a 1.75% increase for 2019 and 1.5%

annual increases for 2020 and 2021. Given long term averages these growth percentages do not appear to be unreasonable.

2017 sales tax receipts, received through the October of 2017 by the ECFSA indicate a 2.83% increase over the previous year. At that rate, the county would break a 5-year trend of budget deficits in this account.

3. ***Overtime*** – Overtime expense rises at a rate significantly higher than the anticipated increase in salaries – 19.37% for 2018 (as compared to the 2017 adopted budget), then 2.1% for 2019, 1.5% for 2020 and 3% for 2021. This is a significant departure from previous budgets and plans that have underbudgeted this expense. The increases, with good overtime management, appear large enough to address ongoing deficits in this account.

4. ***Vacancy Savings*** – The current plan calls for $5.1 million in savings over 4 years - $1.8 million in 2018 and $1.1 million in each of the out years. The previous version of the financial plan had $4.4 million in vacancy savings over the 4-year period, a $700,000 increase. While annual and aggregate figures are very achievable, based upon the county's program of holding positions vacant, the increase in budgeted vacancy savings is a concern, in that it lessens the arsenal the county has to call upon in the event of a shortfall elsewhere in the budget.

5. ***Labor Agreements*** The county negotiated contracts with the Sheriff's PBA and the Holding Center's Teamsters. For 2018 and beyond the county has placed a priority on negotiating expired contracts with CSEA (the county's largest labor union) and AFSCME. Potential negotiated cost of living increases are not included in the financial plan for any of these unions. The ECFSA has not been kept abreast of these negotiations so that it can opine on the financial ramifications.

6. ***Pension Expenses*** – In comparing the current financial plan to the last submission, for the 2018-2020 period pension expenses have increased by $5.8 million for the concurrent years of the forecast. This increase is despite the reduction in the county's pension rates due to attrition in the earlier retirement tiers that are costlier.

7. ***Employee Medical***– Compared to the 2017 Adopted budget submission, employee medical expenses have decreased by $14.5 million for 2018 through 2020. A significant decrease, given the county's anticipated increase in rates.

8. ***Retiree Medical*** – As compared to the 2017 adopted budget version of the financial plan, the county has decreased its estimates for retiree

medical expenses by $11 million for the 2018-2020 period of the plan. A significant decrease, given the county's anticipated increase in health insurance rates.

9. ***Risk Retention*** – In 2016, the county spent $2,973,671 in its risk retention fund. For 2015, the county incurred $3.6 million in Risk Retention expenses. In the previous version of the financial plan, the county budgeted $2 million per year for risk retention expenses, a sum clearly on the lowest end of the scale for anticipated outlays. The current version of the plan increases that amount to $3 million per year, a more appropriate figure.

Gap and Gap Closers

On the most recent version of the plan the county is reporting a smaller gap than in the past - $475,000 in the current submission vs. $7.9 million in the 2017 adopted plan.

The current, stated gaps are as follows:

Year	***Gap***
2019	$ 271,952
2020	$ 104,563
2021	$ 99,159
Total	***$ 475,674***

The county has put forward several potential gap closers including:

- Better than expected sales tax revenue
- Better than expected property tax assessment growth
- Reductions in discretionary spending, including in personal services and deletions of positions
- Employee retirements due to existing union contract provisions and new contracts
- Property tax revenue
- The use of appropriated fund balance
- Participation in the Employer Contribution Stabilization Program
- Greater state reimbursement for indigent legal defense expenses
- More favorable caseload trends in social services programs
- Reinstatement of Gaming Facilities Aid

Potential gap closers are not quantified at this point. Amounts and usage are contingent upon the order of magnitude of fiscal issues the county may face.

5. SUMMARY/RECOMMENDATIONS

The previous ECFSA budget and financial plan report focused on ECMC related IGT and DSH issues that had an order of magnitude to create tremendous financial uncertainty in the county's previous budget and financial plan. Since then, the ECFSA has issued approximately $155 million in bonds to finance certain Hospital capital projects, including a new state-of-the-art emergency room and has refinanced existing capital debt to save the Medical Center tens of millions of dollars in debt service payments, a portion of which, $17 million, has been included in the plan as a revenue source to balance the county's finances.

Credit goes to Hospital and ECMC officials for bring this borrowing to fruition that will help the Medical Center in both a strategic and financial sense.

The impact of ECMC's finances on the county remains a concern for the ECFSA. However, the ECFSA, in its review of the county's 2018 financial plan finds the budget in balance and the county's financial projections, as-a-whole, to be reasonable and achievable.

Given the size and complexity of the county's operations and budget, there are issues the ECFSA would like to comment on that could be problematic for the county going forward:

Erie County Medical Center Corporation

- The $17 million the county has included in its plan from the ECFSA borrowing for ECMC capital projects does help balance the budget, but the opportunity cost is the potential lost savings for ECMC. Given the health care environment in Washington and the challenges ECMC faces as a public hospital, serving the poor and indigent of the county, finances are stable at this point, but ECMC does not have the taxing power afforded to Erie County to alleviate any future fiscal issues. With the contractual ties between the county and the Hospital, Medical Center finances and their potential impact on the county are a concern for the ECFSA.

  Recommendation – Given the contractual relationship between the county and ECMC, and uncertain environment for public hospitals, the ECFSA recommends continuation of the partnership between the two entities that led to the hospital improving its strategic position and saving significant dollars on borrowing through the Authority.

Sales Tax Revenues

- Sales tax is the largest single revenue source for Erie County, encompassing almost 31% of general fund revenues in 2018. Since 2009, when sales tax revenues decreased as compared to the prior year, the county has benefitted from regular increases in this revenue source. Outside of regularly reauthorizing the legislation to maintain this revenue, there is little the county can do to impact its growth. Despite a 5-year trend of budget shortfalls in this account, the county is experiencing a slight overage in this account for 2017 thus far, that should lead to a modest budget surplus at year-end.

- ***Recommendation*** - Given the volatility of this revenue source, and prior overestimations, the ECFSA urges the county to closely monitor receipts and make strategic decisions to maintain a balanced budget in the event that this major item does not meet expectations.

Overtime

- For several years, the county has consistently exceeded its overtime allocation. However, the most recent plan increased 2018 appropriations, the base year for overtime calculations going forward, by almost 20% as compared to the prior year budget. That large increase and subsequent upward adjustments in the overtime budget should be sufficient, assuming good overtime management practices, to eliminate budget shortfalls in this account over the period of the plan.

- ***Recommendation*** - The ECFSA urges the county to continue to closely monitor overtime to provide reasonable assurance that overtime will not exceed the increased budget, while not compromising compliance.

Expired/Expiring Labor Agreements

- Despite the county's goal of settling significant contracts in 2018, the county has not specifically budgeted funds for any potential net settlement costs.

- ***Recommendation*** – the ECFSA urges the county to prepare for potential negotiations with an eye toward further benefit and/or work rule changes that will foster a stable county labor force, while not overburdening county taxpayers.

Vacancy Control

- The increased use of vacancy savings to help balance the budget and plan reduces the order of magnitude of turnover/vacancy savings as a potential gap closer.

- ***Recommendation*** - the ECFSA urges the county to maintain its vacancy control program, while keeping budgeted vacancy savings at minimal levels. In 2017 the county has maintained a program in which between 5-7% of its full time general fund positions remain vacant. Continuation of that program with like vacancy percentages is necessary to balance the plan through 2021.

Pension

- Despite county pension rates going down costs are higher in the current version of the plan as compared to the previous plan. The cause is that the salaries they are based on are increasing due to a combination of higher wages and additional positions.

- *Recommendation* – The ECFSA recommends that the county closely monitor this account and maintain vacancy and other related savings that will mitigate its exposure.

Medical Expenses

- Compared to the Adopted 2017 Budget submission, employee medical expenses have significantly decreased in this version of the financial plan despite increases in anticipated rates going forward.

- ***Recommendation*** - The ECFSA urges the county to closely monitor the implementation of contract provisions and other initiatives to provide reasonable assurance that the order of magnitude of anticipated savings mitigates general health care cost increases.

Staffing

- For the 2018 proposed budget, the county is assuming the addition of 51 positions across all funds, as compared to the 2017 adopted budget. Over the last 5 years, the county has increased its full-time staffing by 178 positions. This additional staffing adds to the county's ongoing spending base, not only in salaries, but fringe benefits, as well

- ***Recommendation –*** The ECFSA urges the county to carefully review any staff additions prior to adding these potentially fixed costs to its budget and financial plan. The ECFSA recommends the county to continue to use technology and management initiatives to “do more with less” and to maintain the management discipline of looking for and implementing efficiencies within functions and departments to further streamline county government.

Fund Balance

- In the most recent version of the plan, the county is continuing to budget \$6 million in fund balance to balance its budget through 2020. In addition, the county is using \$4.26 million per year (\$17 million total) in special fund balance that was generated as part of the ECFSA borrowing for ECMC capital projects. If not replenished, the potential use of these funds lowers the county’s reserves and indicates an imbalance between recurring revenues and expenses.

- ***Recommendation*** - the ECFSA looks to the county to closely monitor expenses and revenues and to review service models to determine the best and most cost-effective ways of providing both mandated and non-mandated services to those impacted by Erie County Government, while maintaining the county’s reserves and to tap fund balance as a last resort.

Health and Human Services Programs

- For the 2018 proposed budget, the county is assuming significant reductions in several Health and Human Service programs including Family Assistance, CWS Foster Care, Safety Net Assistance, Child Care DSS and Children with Special Needs, as compared to the 2017 adopted budget based financial plan. The county has not provided some projections to justify these reductions, but there is a potential for the trends to change over time, thereby creating fiscal issues for the county.

- ***Recommendation –*** the ECFSA recommends the county closely monitor these programs to determine the reasonableness of projections provided and that the county prepare contingency plans to make up potential shortfalls in these account, should anticipated trends not materialize.

ECC Chargebacks

- For the 2018 proposed budget, the county is not charging back \$3.6 million to municipalities for residents who are attending community colleges that are outside of Erie County. This reduces revenues by \$3.6 million.

- ***Recommendation –*** The ECFSA recommends the county look at this practice in-light-of the ramifications it has on this revenue stream and the issue of chargebacks as-a-whole, moving forward.

Risk Retention

- In its current version of the financial plan, the county has increased its budget by $1 million per year, from $2 million to $3 million, as compared to the 2017 adopted budget and plan. This increase more closely aligns appropriations with actual outlays from this account.

- ***Recommendation –*** The ECFSA recommends the county maintain this increased level of funding that more closely approximates actual expenditures.

In closing, we want to reiterate given the extent of the county's services and the size of its related budget, continued due diligence is required to maintain the public services residents of Erie County need and desire and fiscal responsibility to maintain a balanced budget with a reasonable cost to its residents and taxpayers. We urge county leaders to continue to work together in the best interests of the county's residents and taxpayers through the period of this financial plan, and beyond.