

ALEXANDER D. PRIGNANO
Director of Finance



JOHN J. LOMBARDI
Mayor

Finance Department
"Building Pride In Providence"

Memo

To: Michael Clement, City Clerk
From: Alex Prignano, Director of Finance
CC: Mayor Lombardi, Mayor-Elect Cicilline, City Council Members
Re: Finance Department Annual Report
Date: December 24, 2002

Enclosed please find the Finance Department's 2002 Annual Report.

DEPAR. MENT OF CITY CLERK
RECEIVED
8:30 AM
DEC 26 2002

IN CITY COUNCIL
JAN 16 2003

READ
WHEREUPON IT IS ORDERED THAT
THE SAME BE RECEIVED.

[Signature]
CITY CLERK

3000 0 2 1110

DEC 26 2002

[Signature]
TO THE DIRECTOR OF THE
FEDERAL BUREAU OF INVESTIGATION
WASHINGTON, D.C.



Finance Department
"Building Pride In Providence"

December 19, 2002

City Councilman Kevin Jackson
Chairman Finance Committee
Providence City Hall
Providence, Rhode Island 02903

Dear Councilman Jackson:

Please accept this letter as my third Annual Report to the City Council. In this report, I will attempt to inform City Council members of major initiatives that the Finance Department has completed or has underway since my last report, which I submitted in December of 2001.

Foremost, the Finance Department balanced the fiscal 2002 budget. The anticipated budget surplus of approximately \$1,000,000 represents the City's twenty-second consecutive budget surplus and will increase the cumulative fund balance to approximately \$8.3 million. Higher than budgeted collections in Distressed City and Excise Phase-Out state aid programs (\$2.5 million), taxes (\$1.0 million), interest income (\$.6 million), fines (\$.4 million), building permits (\$.5 million), and recorder of deeds fees (\$.3 million), as well as saving from refinancing debt, debt service reserves and interest from debt reserves (\$3.3 million), salaries (\$1.7 million), fuel, snow removal, and refuse processing (\$1.0 million) were the major components of a \$10.2 million positive budget variance in fiscal 2002. However, due to state budget problems and the resulting reductions in anticipated state aid, much of the potential surplus was used to balance the current 2003 budget. In fact, Providence had been averaging nearly a 14% annual increase in state aid over the last five years, but in fiscal 2003, the increase was only 4%. This was the most significant factor in forcing the City to use most of its budget variance from fiscal 2002 in balancing the fiscal 2003 budget.

Another important financial achievement was that an actuarial calculation was performed on medical claims that are incurred but not reported (IBNR). These not yet reported claims each year, as of June 30th, eventually are paid through our health care self-insurance fund the following fiscal year. Reserving \$3.1 million for these claims will prevent future budgets from being negatively impacted by old year expenses, thus creating budget flexibility and more accurately reflecting city finances. With this action, Providence will have a cumulative fund balance of approximately \$8.3 million, will have fully reserved future health care claims, and reserved over \$6.0 in our legal accrual against potential litigation. All of these financial results provide financial flexibility.

Another important responsibility of the Finance Department is making presentations to rating agencies and bond insurance providers. Last June, I made presentations to both Moody's Investors Services and Fitch. Both agencies confirmed the City's bond rating, but due to the lost state aid both required an update once the City Council adopted the fiscal 2003 budget. The follow up presentations occurred last October in conjunction with a Providence Public Building Authority (PPBA) \$31 million school bond issue. The results of the follow up presentations were that Standard & Poors, which only rates the PPBA, issued the Authority a BBB+ rating. The BBB+ rating for the PPBA, which is rated one step below the City's general obligation debt, would translate to an A- rating for the City. Also, both Fitch and Moody's confirmed the City's ratings at A- and Baa1 respectively. All three agencies seemed satisfied with the way a balanced approach was adopted for the 2003 budget. The combination of a tax increase, expenditure reductions, and using a portion of the fiscal 2002 surplus to fill the budget shortfall created by the lost state aid was positively received by the various rating agencies. The credit reports from all three agencies will be available shortly to coincide with the upcoming PPBA school bond issue. Moody's as recently as last June, stated that "Recent City budgets have featured prudent revenue assumptions, necessary tax increases and tightly controlled expenditures. This formula has provided the City with a measure of operating flexibility previous lacking." The FY03 budget includes all three areas positively noted by the rating agencies: conservative budget practices, especially with the collection rate on the tax levy; increased funding to the pension system; and a willingness to increase revenues when needed. Moody's also stated that "debt position was expected to remain manageable given anticipated State support for the school debt construction program." At my suggestion, Mayor Lombardi, last October attended a breakfast with analysts from Moody's in order to assure them that the government was functioning in an orderly manner, that many key members of the City Government were still in place, and that the transition to his administration had been successful. In general, I believe the above mentioned comments in the report were more positive than in previous reports and Moody's has recognized the way the City is dealing with funding the pension system and conservative budget practices. In my opinion, the City's bond rating is stable at this time. It is worth noting that I have asked our financial advisors at First Southwest to explore having Standard & Poors, which I previously mentioned only rates the PPBA's debt, review the City for a possible rating. Standard & Poor's BBB+ rating for the PPBA would translate to an A- for the City's general obligation debt. By achieving an A- rating from Standard & Poors, Providence would have two A- ratings, from S&P and Fitch.

As mentioned in my report last year, I believe once the City gets its pension system issues under control, which includes completing its phase-in to fully fund the pension system based on actuarial requirements; an increase in the City's bond rating could occur. However, newly added debt payments and increased pension cost that resulted from a new contract that eliminated the 6% COLA's going forward in favor of a 3% compounded COLA, all impact the City's fiscal 2003 & 2004 budgets. These costs as well as the pension phase-in and recently negotiated school contract, will require a combination of growth in the tax base, collection rate, tax rate, and/or other revenue sources. In addition, if the State of Rhode Island is unable to significantly increase state aid to Providence, a significant budget shortfall is expected and difficult decisions will

have to be made concerning existing services, programs, and the possible disposition of city assets.

Providence for the third consecutive year issued its citywide audit within the six months allowed by state law. This is noteworthy since these three fiscal years (1999, 2000 & 2001) are the only years I believe the city has issued its audit on time. The fiscal 2002 audit is underway and it is much more complicated this year due to a new accounting pronouncement that was adopted, Government Accounting Standards Board 34 (GASB34). Mr. Shawn Warren, senior partner at KPMG says, "GASB 34 is probably the most dramatic impact on financial reporting ever." This accounting change must be reflected in our financial statements as of June 30, 2002. The Controller, Deputy Controller, and I have been working on this initiative since January 2001, in order to insure that all city departments and agencies (Providence Economic Development Corporation, Civic Center, Skating Rink, Water Board, School Department, Providence-Cranston Work Force Development, and all other departments) will be GASB 34 compliant for this coming audit. GASB 34 requires major changes to the City's financial reporting. For example the City must report infrastructure assets, depreciation will be required on city assets similar to for profit businesses, and long term sick and vacation, as well as long term liabilities (outstanding bonded debt) and infrastructure will need to be included with all other assets and liabilities. In other words, part of the cumulative fund balance. This is important, as failure would result in a qualified audit opinion and could even have rating agency implications. Currently the city has the highest opinion an audit firm can issue, an unqualified opinion on the financial statements and I plan to issue the audit once again in a timely manner. However, I have taken the necessary precaution of requesting a thirty day extension from the State Auditor General in case we need a few extra weeks.

The most time consuming project that the department currently has underway is the implementation of the new integrated software package. As you recall, the project was initiated in fiscal 2001 and began with a complex Needs Assessment of all city departments to determine software requirements. It was determined the software implementation would include the general ledger, payroll, tax billing and collections, tax assessments, retirement, budget, human resources, fixed assets, deeds, voter registration, purchasing and the municipal court. KPMG was selected over four other vendors to assist the city with the Needs Assessment and Quality Assurance during the implementation. As a result of the study, which resulted in hundreds of hours being spent interviewing employees in all city departments, a Request for Proposal (RFP) was developed. The most basic requirements of the RFP required vendors to bid on all the core financials, integrating the Assessor's and Collector's Offices, and having successfully completed a project similar in scope in a city with a total population approximating Providence. The selection process included interviews and demonstrations from four vendors that met the basic requirements of the RFP. At that point, the forty plus employees that attended the demonstrations were asked to rank each vendor's products by functionality and their ability to perform their needed tasks. From the "ranking", the selection was narrowed to two vendors (Eisner Technology Solutions & Munis). After weeks of negotiations between the project team and the two vendors, a decision was made to award the project to Eisner Technology Solutions of New York and

their Lawson software solution. The Lawson software product is a tier one, web based, that allows access to city information through the Internet and was clearly the most technically sophisticated product offered by any of the bidders. It is worth noting that all forty plus employee surveys ranked the Lawson financial solution either first or second. Other software providers that Eisner partnered with for the implementation are "Govern", a Canadian based company for tax assessments, collections, land records and permitting; and Leading Edge's "Ticket Tracker", located in Georgia. Ticket tracker software is being used in eight other Rhode Island Traffic Courts and is fully compatible with the State of Rhode Island's Traffic Court.

Eisner's original bid of \$4.2 million did not include hardware. However, by compressing the implementation process from 20 to 14 months; making available the necessary city personnel or resources, moving the procurement process from a "go live" date of January 2003 to July 2002, which eliminated a costly interface; and negotiating a general price reduction, a new fixed fee contract of \$2,687,000 was agreed upon. It is important to note that this new negotiated contract included the necessary IBM hardware of \$100,000. In addition I was able to negotiate that all future product updates would be included and that all maintenance is capped at not to exceed 5% a year for ten years. I wanted to insure that once we committed to a software package we would not be faced with maintenance contracts that rose significantly each year.

To update you on where the project stands, the City implemented its general ledger, accounts payable, accounts receivable, grants, tax assessments, tax collections and state tickets at the municipal court in July. On August 26 all departments were required to use the new e-Requisitioning software. The financial applications that went live in the Controller's Office were more in my control and though they are still on the expected learning curve they are operating the new software packages.

The Purchasing module affects all city departments. The training of all requisition users and department heads, which now approve purchase requisitions online, has taken longer than expected and has required additional training. Approximately 350 users will be using this software between city departments and schools, and I have established a help desk in Data Processing to assist with e-Requisitioning. Fixed Assets is part of the purchasing module and will be live later this fiscal year and in full operation.

A decision was made to delay the budget module in order that the budget personnel in my office and the school department will receive training just prior to beginning the fiscal 2004 budget process. With a "go live" date of July 2002 and the budget submission charter requirement being May 2nd, the 2003 budget was prepared on the existing system. However, the budget has now been loaded into Lawson and we are learning how to create and modify reports.

The Assessor's and Collector's Offices tested for several weeks and were anxious to move to the new Govern software. The Assessor's Office has had to use the existing Data General System as well as the revaluation company's Universe software in order to produce a tax roll. The inputting of tax receipts and business procedures will be

streamlined in the Collector's Office and workflow for both departments will be smoother with the Govern software.

The "Ticket Tracker" system at the Municipal Court has required much more training than was anticipated. The Court personnel felt that specific business practices unique to the Court needed developing. These practices include interfaces to collection companies, special reports for the boot squad, the ability to track tickets specifically the way court personnel desired, and building an interface to handheld ticket devices. The police department has been in the process of procuring the purchase of handheld devices for over a year and this has caused delays. Handheld computerized ticket units eliminate the need for data entry of thousands of written tickets. Without these devices, tickets have had to be entered manually, and the volume has resulted in the Court being approximately 6-8 weeks behind in processing tickets. This has affected the "go live" date for Ticket Tracker with city citations. Several months ago, I instructed members of my staff to follow up and assist in getting these devices purchased and online. Currently a decision has finally been made on the specific unit we will purchase and my understanding is the units should be received any time now. This delay, as well as the need for additional training and developing specific business procedures have resulted in additional cost of approximately \$80,000 to the project and have delayed the "go live" date until February.

In addition to the \$80,000 for Ticket Tracker, I have gone to the Board of Contract and Supply for approximately \$60,000 for additional support and training in both the Lawson and Govern applications. In total, the project has had approximately \$140,000 in change orders mostly due to the need for additional training and support for city personnel who have had some difficulty in learning the new applications. However, the amount in change orders to date is relatively small on a software implementation of this magnitude.

The second phase of the project is underway and includes city, school and retirement payrolls, human resources for city and schools, land records, mass appraisal, Geographical Information Systems, e- Commerce, as well as inspections and permitting. The human resources and payroll phases have begun but the schedule has proved to be too aggressive. The Controller's staff is still on a learning curve for phase one, as well as focusing on the citywide audit. In addition, the prior Personnel Director was out of work all summer due to surgery and has left city employment. It is not realistic to have a temporary Personnel Director get involved with the project at this time. I have had discussions with Eisner's Project Manager regarding delaying the payroll and human resources implementation until April. This seems more realistic considering city resources available. The new strategy is for Eisner to provide additional resources and to build and deploy the payroll system with assistance from city staff. This will result in a second change order of approximately \$90,000. I expect that the overall cost of this project will remain under \$3.0 million, which will still be more than a million dollars less than the original bid.

The Mass Appraisal implementation, which must be in place for the upcoming statistical update that will be reflected in the July 2004 tax bills, has just begun. The Request for Proposal to advertise for a vendor to implement the "update" will be at the Board of

Contract & Supply on December 30th. However, once again city resources are negatively impacting our mass appraisal implementation. Currently the Assessor's Office has three union Appraiser positions funded that require specific certifications. These positions were created nearly two years ago and we have been unsuccessful in filling them. The qualified applicants who have responded to our employment ads all lived outside Providence and were not willing to relocate. There are other appraiser positions in the department that over the years have been filled with senior office workers; however, these employees are not certified appraisers. Recently, Local 1033 and the Cianci Administration entered into a memorandum of agreement assigning two individuals into appraiser positions that created four non-certified appraisers. Also, four other individuals were promoted that have disrupted the business flow of the office. I did not want to implement the agreement, contesting that the individuals did not possess the bare requirements of the positions; however, the current administration determined the memorandum of agreement valid and implemented it. We had held off mass appraisal until there were sufficient human resources. However, we cannot hold off any longer in order to complete the statistical update on time. This has resulted in only the Deputy Assessor being trained on the Govern mass appraisal product. This is a key issue that needs resolving.

The GIS component of the Govern software requires a city resource person that can build and deploy GIS capabilities in each city department. The Police and Fire Departments require different information than Parks and Public Works. The City needs to hire someone with GIS capabilities to move this portion of the project towards completion, and to be able to map and keep accurate information once the consultant is gone. I have read the Cicilline Administration is partnering with the Providence Plan in order to develop GIS capability and to create a database similar to Com-Stat in New York City. I believe Mayor Cicilline wants to create a database called Prov-Stat that will possibly eliminate the need for a city GIS resource.

E- Commerce is proceeding cautiously, as the Web Master for the City has been working towards providing the ability for residents to pay taxes and access tax information online. However, though the Web-Master is exploring options, until I am comfortable with security issues that will arise from this online capability and until more important Govern modules are operational (i.e. mass appraisal), this is a low priority.

The inspections and permitting phase of the implementation has also not started. I am concerned with spending funds and committing resources to a department in which all the key personnel that participated in the Needs Assessment and selection process have left city employment. Currently I do not know if the department has the employees with the proper skill sets to undertake the necessary implementation requirements.

The Recorder of Deeds Office was to "go live" with land records in phase one. This was delayed at the time of training due to the lack of computer literacy in the department. Even after receiving training on basic Word Functions and training by the Govern technician, the employees seemed unable to operate. These employees are receiving additional training in order that deeds, assessing and billing will all be integrated. In fairness I must report, the Recorder of Deeds does not believe computer literacy was the

problem. This is now becoming a priority for the project and we hope to have this functional in the very near future.

Though there are concerns and delays, the City did manage to “go live” with the general ledger, purchasing module, assessments, billing and collections and is proceeding with human resources and payroll. Considering the magnitude of the project, the implementation is going as well as could be expected. The key components of the project will be completed in a reasonable timeframe and without the horror stories everyone has heard concerning cost overruns that approach the dollar amounts of the original contracts. However, where delays have occurred it has been a matter of not having the necessary city resources or personnel with the skills to handle the necessary tasks.

The Finance Department has prepared a Five-Year Financial Plan that will be submitted to the City Council this month in accordance with the City Charter. I believe the FY2003-2007 Plan reflects conservative revenue assumptions based on state aid that was received in fiscal 2003 and the State of Rhode Island’s Five Year Plan for state aid. Due to this conservative approach and no new revenue sources included, the Plan reflects significant budget shortfalls. This illustrates the need for Providence to be allowed to create new sources of revenue such as selective municipal fees (entertainment tax, meals and beverage tax), broad based taxes (occupation tax), and/or payments from the tax exempts. Also, the Plan demonstrates the need to finally address major expenditures that affect the budget such as healthcare costs and pension contributions.

I am currently in the process of two major initiatives: refinancing Prov-Port debt and attempting to reduce healthcare cost by reducing the administrative fees the city pays to have our health plan administered by Blue Cross.

The Prov-Port debt refinancing would allow the city to be repaid the \$900,000 that was paid to replenish the debt service reserve account that was charged to make debt service payments for Prov-Port in fiscal years 2002 & 2001. The refinancing would also be structured to make enough of the saving available in order to dredge berths that would allow for potential new business. The debt service payment schedule would not be extended and would still be completed in September of 2024. The annual debt payments would be slightly reduced, the city would receive \$900,000 and the port would be provided the necessary funds for dredging. However, the refinancing will only work if Prov-Port can secure insurance on the bond payments. I have told Prov-Port officials the city would not be willing to secure the debt, thus the need for the insurance. Currently, Radian, an insurance provider is reviewing Prov-Port’s financials, leases and budgets and we expect to know whether this is a possibility no later than January.

The healthcare initiative could save \$4 - \$5 million over the next four years. United Healthcare was asked to discuss the possibility of administering our health plan and they have provided the city with a very attractive proposal. However, to move to United Health the city must complete negotiations with the firefighters or have the firefighters agree to use a different provider other than Blue Cross which is specified in their current contract. Currently all other contracts allow for the changing of healthcare providers if the coverage is identical to the contracts that cover current and retired employees, which

United Health has guaranteed. This issue needs immediate attention from the incoming administration, and I would be happy to brief members of the City Council in detail.

I also want to report on some of the activity of the divisions that are part of the Finance Department (Assessor's Office, Collector's Office, Controller's Office and Data Processing).

The City Assessor's Office implemented the citywide revaluation that was reflected in tax bills mailed out a year ago last August. The revaluation, combined with changes in assessments the City Assessor has made since the mid 90's, has led to an overwhelming number of lawsuits with commercial taxpayers. In fact, the law suits and potential suits have overwhelmed the office. There is little ability to handle these appraisals in house due to the lack of professional staff, thus I have enlisted the assistance of an outside appraisal firm to help us defend the City Assessor's actions on pre-revaluation increases to assessments. I hope this action will short circuit some of the appeals that could lead to further litigation if not resolved. As far as appeals that stem from the revaluation, Cole, Layer & Trumbull will, by contract, defend the values placed on these properties. It has come to my attention over the last several months from conversations with the City Solicitors who are handling these tax cases, that the Assessor's Office had resisted meeting with many of these commercial property owners. By meeting with these property owners, a line of communication would have been created and many of these law suits could have been avoided. However, this did not happen, and it was a major mistake that will not occur again. The City Assessor in the future will meet and attempt to explain reasons for increases in assessment to taxpayers. These numerous law suits, as well as normal revaluation appeals, previously mentioned vacancies and the memorandum of agreement have all negatively impacted the effectiveness of the office. The need for adding professional staff has reached a critical point in this office.

The City Collector has continued to employ a firm but fair approach in dealing with taxpayers. Unless an individual is experiencing a financial hardship, payment plans are not granted and interest is not waived. Also, the taxpayer must provide evidence that demonstrates the financial hardship. Once a payment plan is allowed, the department monitors the plans in order to assure the conditions of the plans are being met.

The personnel in the Collector's Office are adjusting quite well to the new Govern software. We experienced a problem with Fleet Bank having the scan line on the tax bills operational with the new software. This caused all bills to be processed in the Collector's Office for the first two quarters. The result was a backlog in processing payments which was not eliminated until November. However, the staff has caught up and now is preparing to send out delinquent notices and prepare for the third quarter's tax payments and begin the preliminary work on the upcoming tax-sale. I am hoping to find an individual with a legal background to start doing some of the collection work we are sending to private collection companies. I believe the right individual could save us significant dollars by doing much of this collection work in-house. The position is funded in the current budget.

Another department under the Finance Department is Data Processing. The department has six employees, with one of those employees now taking on the role of being the Lawson software Help Desk for procurement. The department maintains the public safety network, a wide area network that has nine local area networks, as well as approximately 500 personal computers and 100 printers. The department also maintains the firewall to protect the networks from viruses and hackers. This is necessary because of Internet activity which is needed to run Lawson's web-based software. The employees in this department have done an adequate job considering the level of experience most of them have. My goal here is to hire a Data Processing Director to further develop the employees and to maintain the needed technology to run the multi-million dollar systems the city operates in both public safety and financial modules. I

The last department that is part of Finance is the City Controller's Office. All retiree benefits, accounting, payroll and accounts payable are the responsibility of this department.

The Controller's staff deserves credit for completing the 2001 City Annual Audit within the six months allowed by the State, and the Single Audit and Management Letter within the nine months allowed. In fact, we have focused on the management comments contained in the Single Audit and last year's audit finding were reduced to only nine comments and two of those were positive comments praising the effort that has been made in issuing timely financial information despite the complexity of the audit.

I had the Controller's Office and Deputy Director of Finance assume responsibility for the financial records and checkbook of the Fleet Skating Center. The personnel at the rink had no accounting expertise and their records were in poor condition which led to audit problems and internal control concerns. Last summer the Skating Center Manager was instructed that approval for all spending must come from the Finance Department and deposits were to be made into a checking account for which the Controller and Treasurer were the authorized signatures. This help to prevent the Skating Center from running a deficit last year by controlling expenses and monitoring revenues. The responsibility for the skating rink has now been assumed by the Civic Center and the General Fund will have to assume the expenses incurred by the rink last summer before the skating season began. I estimate the total of these bills, which would have been paid by skating proceeds which are no longer available to us, to be approximately \$25,000. However, the one year we were involved, the skating rink ended the fiscal year with a positive cash balance of approximately \$80,000 and all debt service payments were current through October of 2002.

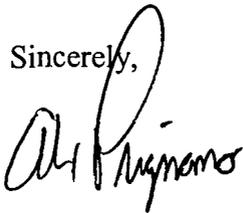
As it is now, the Controller's Office with only six professionals is understaffed. City departments and agencies that receive funds from the City are numerous, and need to be monitored more directly. However, with a Controller, Deputy, and four accountants it is impossible to get involved as thoroughly as we would prefer. When you consider all the funds that exist in the City (general fund, schools, capital projects, trust funds, pension

system) and all the satellite agencies (Providence Water, Public Building Authority, Civic Center, Skating Rink, Community Development Grants, Drug and Alcohol Grants, Housing Corporation are some) and all require extensive interaction and review by both the Finance Department and Controller's Office.

In closing, my major theme continues to be the need for additional professional staff. I want to thank this City Council for funding professional positions that I have requested in prior budgets, and I am hopeful that the new administration will support and assist me in recruiting the needed resources to improve the functionality of the Finance Department.

I have attempted to address what I believe are the major initiatives currently underway in the Finance Department. I hope this, my third report, provides you with an idea of some of the Finance Department's accomplishments, as well as some of the problems we are experiencing.

Sincerely,

A handwritten signature in black ink, appearing to read "Alex Prignano". The signature is written in a cursive, somewhat stylized font.

Alex Prignano
Director of Finance

Cc All City Council Members
Mayor Lombardi
Mayor-Elect Cicilline
Thomas O'Connor
Stephen Key