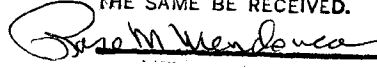


No. 43

IN CITY COUNCIL
JAN 15 1981

WHEREUPON IT IS ORDERED THAT
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INTERIM REPORT

The Mayor's Advisory Committee on Finances

January 1981

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RHODE ISLAND PUBLIC EXPENDITURE COUNCIL

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M E M O R A N D U M

TO: Mrs. Rose Mendonca
City Clerk

FROM: Gary S. Sasse, Chairman
Mayor's Advisory Committee on Finances

DATE: January 10, 1981

Enclosed are copies of this Committee's Interim Report. At the request of Mrs. Brassil, Chairman of the City Council's Finance Committee, I am asking that you distribute these copies to all members of the City Council, except the following members who have received their copies:

Mrs. Brassil
David G. Dillon
Malcolm Farmer, III
Robert F. Lynch
Charles R. Mansolillo

INTERIM REPORT

The Mayor's Advisory Committee on Finances

I. General Findings

Immediate steps must be taken by the Mayor to present and the City Council to adopt a balanced financial plan for the current fiscal year ending June 30, 1981, in order to avert a fiscal crisis. If steps are not taken,

- The City of Providence's potential operating deficit for this year could total approximately \$24 million, thereby increasing the accumulated operating deficit at the close of the fiscal year from over \$14 million to an estimated \$38 million.
- The City will probably run out of cash in the early part of May 1981 and will experience temporary cash shortfalls in the interim. Under existing City Charter provisions, Providence is not in a position to borrow sufficient funds to continue operations for the remainder of this fiscal year.¹
- In view of the urgency of the financial problems facing the City of Providence, action is needed by the Mayor, City Council and State Legislature within the next thirty days to implement the Plan of Action in this Report.

The Committee finds that longer-range solutions to the fiscal problems of the City of Providence require that:

- Effective management, spending control, and budgetary procedures and conservative budget forecasting techniques be implemented by the City administration. There can be no substitute for sound fiscal management and budgetary control.
- Additional revenue sources to the property tax be quickly explored to fund City services. The property tax base presently grows by approximately 2% per year in Providence, while the City is faced with double digit inflation. With excessive reliance on property taxes, the tax base could decline and the City's financial condition will deteriorate even further. However, development of alternative revenue sources will require time and cannot be expected to meet required needs in the current fiscal year.
- Limits must be placed on the level of growth in City and school spending, which may require a reduction in service levels.

¹Projection based on the City Controller's cash flow estimates for fiscal year 1981 assuming all bills are paid.

II. Current Fiscal Condition

The original budget estimates for fiscal year 1981, as submitted to the City Council in the spring of 1980, projected that the City's total general fund and water revenues would total \$121.6 million.² Revised revenue estimates indicate, however, that total general fund and water revenues will produce only \$105.3 million in the current fiscal year. As shown in Table I, revenues are now projected to yield \$16.3 million less than originally budgeted for fiscal year 1981.

On the expenditure side, the Mayor originally proposed total general fund and water expenditures for fiscal year 1981 of \$121.6 million.² However, as shown in Table II, total expenditures for fiscal year 1981 are now projected to total \$129.5 million, or \$7.9 million more than originally proposed.

When the projected \$16.3 million over-estimate of revenues is combined with the \$7.9 million under-estimate of expenditures, a revenue/expenditure shortfall of \$24.2 million is now projected for the current fiscal year.³ It is possible that the projected shortfall in the water department can be offset by additional water revenues, but the estimated fiscal year 1981 operating gap would still approximate \$23 million (see Table III).

In order to offset a projected FY1981 operating shortfall of \$24.2 million, without any of the other steps set forth in the Plan of Action below, an additional tax of \$24.60 per \$1,000 assessed valuation would be needed to secure a balanced budget for the current fiscal year, as shown below. (This assumes continuation of the City's present modified cash accounting system, and an estimated 75% collection rate on any supplemental tax payable by June 30, 1981.)

²Revenues and expenditures do not include \$17.8 million in state and federal aid for education.

³This does not take into account actions being taken or to be taken by the administration to reduce spending in fiscal year 1981.

Assessed Valuation, 12/31/79

Excluding Machinery & Equipment	\$ 1,322,947,951
Assessed Value of Abatements	(10,039,160)
	<u>\$ 1,312,908,791</u>
Value Per \$1.00 Tax	1,312,908
Additional Tax Rate	<u>24.60</u>
Levy	\$ 32,297,537
Collection Ratio	<u>75%^a</u>
Amount to be Collected	\$ 24,223,153

^aEstimated 75% collection would require a \$24.60 tax rate. Such a collection ratio would be more conservative than a 89% collection due to a possible high delinquency rate, but even 75% cannot be guaranteed. Additional revenue might be collected if the penalty on delinquent taxes were raised to current market levels and a tax sale held before fiscal year's end.

However, the Committee believes various steps can be taken to reduce this financial burden on property taxpayers as outlined in the following Plan of Action.

III. Plan of Action

A \$24.60 or 44% property tax increase, six months into the fiscal year would create significant hardship for property taxpayers in the City of Providence. Recognizing this condition, the Committee believes that a three phase Plan of Action which includes the following interrelated and dependent components should be considered as an alternative to either a \$24.60 property tax rate increase collectible prior to June 30, 1981, or an unbalanced operating budget and potential municipal insolvency. The Plan of Action involves three phases: Fiscal Year 1981, Fiscal Year 1982, and longer-range steps as presented below.

A. Phase I: Fiscal Year 1981

The City Charter requires the Mayor and City Council to prepare and adopt a balanced fiscal year 1981 budget and financing plan. In this regard, the Committee recommends the following plan: to change the accounting system; to reduce projected expenditures; and to fund the remaining operating shortfall through a supplemental tax increase payable over six installments.

1. Implementation of effective budgetary procedures to monitor, control and limit departmental spending. As noted in the section entitled "Current Fiscal Condition," the City of Providence faces a potential shortfall of \$24.2 million in fiscal year 1981. Even at this late date the Finance Director and the Committee believe that this gap can be reduced by an estimated \$4 million as a result of:
 - a. Action by municipal departments to cut expenditure rates from current levels;
 - b. Savings resulting from recent City layoffs;
 - c. A reduction in the amount required to fund prior year deficits if a modified accrual method of accounting is implemented; and
 - d. Establishing the Water Supply Board as an enterprise fund with the City being reimbursed for services rendered to the Board.
2. Adoption, with the Rhode Island Auditor General's approval, of a modified accrual method of accounting in the current fiscal year.

The City's current method of financial reporting recognizes expenditures when paid or incurred. Revenues are recognized only when received and not when levied or measureable as required by generally accepted accounting principles as they relate to municipalities. For each of the past several years the City's independent auditors have recommended that Providence should change to a modified accrual method of accounting.

In the absence of this accounting change the City would have to both levy and collect sufficient revenues to balance the budget by June 30, 1981. By making the change to a modified accrual method of accounting the City can levy a supplemental tax, have it payable over a longer period of time, and can borrow against anticipated tax collections to the extent prudent and necessary.

It is necessary for the City to change its method of financial reporting from the present system to a modified accrual system that recognizes income when levied (less an amount determined to be uncollectible) in order to minimize the property tax increase needed to bring the fiscal year 1981 operating budget into balance. Implementation of this method of accounting will more properly recognize revenues when available to finance current year operations.

One of the effects of a change to a modified accrual from a modified cash method of accounting would be to reduce the accumulated deficit at June 30, 1980 from approximately \$14 million to approximately \$4 million. This is based on City estimates of net collectible receivables of approximately \$10 million at June 30, 1980. The change would have very little effect on the projected shortfall for the current fiscal year. The major difference on current year's operations would be to enable the City to record approximately 96% of the supplemental levy as revenues for the current fiscal year rather than only the amount collectible by June 30, 1981.

3. A \$16.00 supplemental property tax increase be immediately adopted to generate an additional \$20.2 million (\$1,312,908, value per \$1.00 tax, x \$16.00 = \$21,006,528 x 96% collections = \$20,166,267).⁴

The \$16.00 increase should be payable over six installments, with \$6.00 due and payable prior to June 30, 1981, and with the remaining \$10.00 payable in four installments through June 30, 1982.

Adoption of this tax adjustment program would result in the following situation:

<u>Property Taxes</u>	<u>FY1980</u>	<u>FY1981</u>	<u>FY1982</u>
Existing Tax Rate	\$ 56.18	\$ 56.18	\$ 72.18 ^a
Supplemental Tax	-	16.00	-
Total Property Tax Rate	\$ 56.18	\$ 72.18	\$ 72.18 ^b
Total Tax Payments Due Per \$10,000 Assessed Value	\$561.80	\$621.80 ^c	\$821.80 ^d

^aIncludes existing \$56.18 tax rate plus \$16.00 proposed increase in FY1981.

^bIf alternative revenue sources and reduction in City services (see Phase II) do not result, additional property tax increases will be needed in FY1982.

^cIncludes only \$6.00 of the \$16.00 suggested property tax increase.

^dIncludes \$10.00 per \$1,000 assessed value accrued and collectible from FY1981.

⁴During the past ten years the City established a trend of collecting approximately 89% of current property tax revenues and 7% in subsequent years. Under the modified accrual method of accounting, it is, therefore, proper to include the total amount deemed collectible.

Levying a supplemental property tax in Providence will require approval of the General Assembly. Section 44-5-1 of the Rhode Island General Laws essentially provides for a city or town to impose a tax for the expenditure of money and to levy a tax on the ratable property of the town.

According to bond counsel, the act is unclear as to whether cities and towns are restricted to one levy. The original levy cannot be changed, but there appears to be no restriction for a second or supplemental levy. In order to ensure the legal basis for a supplemental tax levy and satisfy bond counsel, it is, therefore, recommended that enabling legislation be sought from the Rhode Island General Assembly to provide for a supplemental tax. Such a tax would be exempt from Section 44-5-7 which provides for an option for payment in equal quarterly installments so that the supplemental tax may be payable in six installments over two fiscal years.

Also, Section 44-5-9, which provides for an interest penalty ceiling, should be amended so that the City may adjust the 8% penalty to a more realistic level in order to encourage the collection of taxes currently due.

4. The current borrowing provision of the City's legislative Charter should be amended by the General Assembly in order for Providence to be in a position to borrow the full amount of the recommended \$16.00 supplemental tax increase in anticipation of collections.

Section 45-12-4 of the General Laws of Rhode Island, entitled "Borrowing in Anticipation of Taxes," essentially provides that any city or town may borrow up to the total tax levy of the then current fiscal year. Such notes may be made payable not later than one year from their date, but may be renewed or paid by the issue of new notes.

Section 6.26 of the Providence City Charter relating to tax borrowing should be amended by the Rhode Island General Assembly because it restricts the City's ability to borrow sufficient cash when the City has a deficit. The City may only borrow up to 80% of available tax revenues as estimated in the budget. Additionally, all receipts and revenues must be fully escrowed to pay the notes under current provisions.

If Providence were allowed to borrow under 45-12-4 as other cities and towns, it could immediately borrow the entire cash flow deficiency.

B. Phase II: Fiscal Year 1982

As soon as the fiscal year 1981 budget is adopted, work must immediately begin to develop and prepare an operating budget for fiscal year 1982 (July 1, 1981, through June 30, 1982).

In developing the fiscal year 1982 budget, the Committee believes that specific policy objectives must be established if additional substantial future property tax increases are to be avoided. The Committee, therefore, recommends the following:

1. Alternative revenue sources to supplement the property tax should be sought. As noted above, it is unrealistic to expect the City of Providence to continue to provide services at current levels when its property tax base increases by approximately 2% annually in a period of double digit inflation. According to the Advisory Commission on Intergovernmental Relations, property taxes account for 79.7% of local tax collections in the nation; in Rhode Island they equal 99.1% of local tax collections.

At this point in its deliberations, the Committee has not had the time to study nor does it endorse specific revenue alternatives. However, it is studying the feasibility of seeking enabling legislation, including one or more of the following:

- a. A municipal payroll tax;
- b. A municipal income tax;
- c. A municipal sales tax;
- d. Gross receipts tax;
- e. Payments in lieu of taxes from tax exempt institutions;
- f. Payments for services rendered to the state government.

In addition, a complete analysis of the City's fee structure should be conducted to determine if additional revenues might be generated from non-property tax sources currently available to the City.

2. A limit should be placed on future spending growth. In view of the City's serious financial condition and until further analysis can be made, the Committee recommends that expenditure growth for both general municipal purposes and schools from all sources not exceed current year spending by more than 5% (excluding welfare and water expenditures).
3. Immediate discussion should commence with the School Committee so that timely action can be initiated by the School Department

to comply with the spending limitations suggested in light of the March deadline for contract renewals. Cooperation with the School Department is vital because general funds for schools totals 29% of general fund expenditures (see Table II).

Specific Committee recommendations to implement the policy objectives outlined in Phase II will be presented to the Mayor the first week of February, 1981.

C. Phase III: Long Term Management Reforms

1. Consideration should be given to a private sector analysis of City management practices and operations during Phase III of the Plan of Action. Under the auspices of the Rhode Island Public Expenditure Council and the Greater Providence Chamber of Commerce, the required funds and necessary loaned executives could be secured from the business community to conduct a general study of the City's management.

This study would not only be useful to the Mayor and City Council in ensuring greater economy and efficiency in the City's delivery of services, but also in preparing to implement the new Providence Home Rule Charter.

For example, private sector managers could review the City's existing management systems in such areas as financial and cash management, purchasing, data processing, personnel administration, general services, interdepartmental coordination, and administrative and management coordination between the School Department and general municipal government. The results of such a management study would include a description of existing practices, findings as to the efficiency and effectiveness of these practices, and, where appropriate, recommendations as to what actions the City might consider to strengthen administrative procedures and organization.

The identification of existing or potential problems in these and other areas would assist the City in its ongoing efforts to strengthen budgetary control and to live within future limitations on spending growth. The forthcoming reorganization of City governance under the provisions of the Home Rule Charter should also provide a good opportunity to implement the recommendations that might result from such a management study in Providence.

2. Finally, to assure that all property taxpayers are treated equitably, property tax valuations should be kept as current as possible. The Committee, therefore, recommends that property assessments be updated more frequently than every ten years as required by state law.

Table I

City of Providence
Fiscal Year 1980-81
Financial Estimate
Revenues (\$ in thousands)*

	<u>Original Budget Estimate</u>	<u>Estimate as of 12/29/80</u>	<u>Difference</u>
<u>REVENUES:</u>			
Property & Excise Taxes			
Current Year	\$ 70,137	\$ 66,849	\$ (3,288)
Prior Year	4,450	5,000	550
Recovery of Abated Taxes	-	82	82
Shared State Taxes			
Liquor	24	24	-
General	716	716	-
Jai-Alai & Dog Racing	426	426	-
Business & Non-Business Lic.	612	615	3
Sewer Assessments	3	-	(3)
Fines, Forfeits & Escheats	725	725	-
Grants-In-Aid:			
G.P.A.	8,000	8,000	-
School Construction	-	388	388
Payments in Lieu of Taxes	3,194	3,194	-
Donations	613	8	(605)
Rents and Interest	2,190	1,535	(655)
General Departments	6,937	3,970	(2,968)
Sewer Rentals	550	550	-
Federal Revenue Sharing	4,904	4,740	(163)
Sale of City Property	5,200	130	(5,070)
Total General Fund Revenues	\$108,681	\$ 96,952	\$ (11,729)
Water	12,914	8,300	(4,614)
TOTAL REVENUES	\$121,595	\$105,252	\$ (16,343)

*Source: City Finance Department

Table II

City of Providence
Fiscal Year 1980-81
Financial Estimate
Expenditures (\$ in thousands)*

<u>Major Expenditure Areas</u>	<u>Original Budget Estimate</u>	<u>Estimate as of 12/29/80</u>	<u>Difference</u>
Executive, Legislative, Judicial	\$ 1,749	\$ 2,391	\$ 642
Finance Administration	2,275	2,275	-
Public Safety - Police	10,678	10,804	126
- Fire	10,960	11,000	40
- Other	1,631	1,638	7
Building Codes - Inspection	627	627	-
Public Works - Sewage Disposal	3,016	4,000	984
- Waste Collection	2,841	3,272	431
- Highway	2,453	2,541	88
- Other	5,312	5,561	249
Recreation - Normal	475	530	55
- Seasonal	412	912	500
Public Property and Parks	5,061	6,117	1,056
Public Schools	31,321	34,505	3,184
Other Departments:			
Planning & Urban	1,163	1,030	(133)
Other	984	1,079	95
General Public Assistance	8,017	8,017	-
Pensions	9,120	9,120	-
Debt Service	7,497	8,302	805
Miscellaneous - FICA	1,124	1,039	(85)
- Blue Cross & RIGHA	2,265	2,063	(202)
- Unemployment Tax	260	260	-
- Reserve for Prior Yr. Def.	1,200	1,200	-
- Reserve for Abatement	400	300	(100)
- Miscellaneous	437	437	-
Grants	1,101	1,101	-
Public Celebrations	17	17	-
Total General Fund Expenditures	\$112,396	\$120,138	\$ 7,742
Water	9,198	9,331	133
TOTAL EXPENDITURES	\$121,594	\$129,469	\$ 7,875

*Source: City Finance Department

Table III

City of Providence
Fiscal Year 1980-81
Financial Estimate
Summary (\$ in thousands)*

	Original Budget <u>Estimate</u>	Estimate as of <u>12/29/80</u>	Difference Favorable (Unfavorable)
<u>REVENUES:</u>			
Before Water	\$108,681	\$ 96,952	\$(11,729)
Water	12,914	8,300	(4,614)
After Water	121,595	105,252	(16,343)
<u>EXPENDITURES:</u>			
Before Water	112,396	120,138	(7,742)
Water	9,198	9,331	(133)
After Water	121,594	129,469	(7,875)
<u>NET:</u>			
Before Water	(3,715)	(23,186)	(19,471)
Water	3,716	(1,031)	(4,747)
After Water	1	(24,217)	(24,218)

Note: Expenditures include \$1.2 million reserve provision for absorbing portion of prior year deficit.

*Source: City Finance Department.