Special Budget, Finance & Economic Development Committee

April 30, 2019

Summary and Motions

Committee chair, Amanda Bledsoe, called the meeting to order at 1:04 p.m. Committee members Steve Kay, Richard Moloney, Chuck Ellinger, James Brown, Susan Lamb, Bill Farmer, Angela Evans, Fred Brown, and Jennifer Mossotti were in attendance. Councilmembers Kathy Plomin and Jennifer Reynolds were in attendance as non-voting members.

I. Approval of March 19, 2019, Committee Summary

A motion was made by CM Farmer, Jr. to approve the March 19, 2019, Budget, Finance & Economic Development Committee Summary, seconded by CM Ellinger. The motion passed without dissent.

II. Financials Update – March 2019

Rusty Cook, Director of the Division of Revenue, reported the comparative unemployment rates through March, with Lexington at 3.5 percent, Lexington MSA at 3.6 percent, Kentucky at 4.0 percent, and the U.S. at 3.8 percent. He reviewed Fayette County's economic indicators, reporting quarterly employment at 194,500 in September (an increase from June). While discussing LFUCG's top four revenue sources, he pointed out the significant variances (month to date) under insurance and franchise fees are because of the timing of three payments and when those payments were budgeted. He said the top four revenue sources are $6.4 million below budget. When comparing current year to prior year he noted we are seeing more tax returns filed early. CM Moloney confirmed LFUCG remains about $4 million short, overall. Cook added that they are still seeing growth but at a lower rate than what was projected for FY19.

Melissa Lueker, Director of Budgeting, reviewed the other revenue categories. She reported the total revenue at a negative variance of $4.7 million. She said she expects the personnel variance to remain positive due to the funds encumbered under personnel. She pointed out how those vacancies were incorporated into the FY20 proposed budget and the need for them to remain vacant. She highlighted the variances under debt service and capital. She said the total fund balance (year to date) is $9.3 million and explained how that money is needed to cover $2 million for debt service, plus the revised FY19 revenue estimate of a negative $6.5 million. She said an additional $2 million is needed to end the fiscal year with a $5 million fund balance, which is necessary to cover PO rolls, grant match rolls, and the FY20 beginning balance of $1.5 million.

Moloney talked about the way the city is cutting expenses to support our revenue and how the numbers presented, particularly $14 million saved in expenses, are perceived by employees who are not slated to receive a raise in FY20. He said he likes the state's approach to creating the budget from zero on a two-year cycle; which could be ratified each year to meet local requirements. He said this sends the wrong message to taxpayers and employees and suggested we reflect on how we use revenue. He concluded that the city doesn't really have $14 million available. CM Bledsoe said she plans to place a conversation about a two-year budget cycle in committee.

CM F. Brown said the focus should be on the change in fund balance of about $9 million. He asked how the personnel variance will play out through the end of the fiscal year. Lueker broke down the funding components of the personnel variance, including overtime and insurance subsidies. F. Brown concluded that this variance could grow. He asked about the negative revenue variance of $4.7 million and confirmed the projection to end the year with an overall change in fund balance of $5 million while taking into consideration a revised revenue projection. He recalled the Mayor's expressed interest to reallocate some of the potential FY19 fund balance to increase employee salaries.

VM Kay talked about a potential fund balance, the lack of raises being included in the Mayor's proposed budget and how that is explained to employees. Lueker explained a fund balance of $5 million is necessary to apply to existing assignments and that if the budget concluded right now there would not be excess fund balance available for other projects. They concluded, year to date, the current balance of revenue over expenses is $9.3 million. Lueker explained some of the timing issues that will impact the $9.3 million, as well as specific uses of the funds. She estimates the operating variance to continue to see positive growth. Kay confirmed the FY20 budget was built based on a 15 percent reduction to all divisions but it was up to individual divisions where to make those cuts. He asked what the difference is between operating expenses budgeted for FY19 and proposed for FY20. Lueker pointed out that it won't be 15 percent because there are other types of accounts that have increased expenses.

Moloney pointed out that costs will continue to grow each year and the need to find money to keep up with increasing costs. He said the comparison of the current year to prior year does not paint out an accurate picture of the current budget. Bledsoe confirmed operating expenses are still encumbered until the year-end. Lueker concluded her presentation comparing revenue and expenses (current year to prior year) pointing out that operating remained the same, which means that we may have budgeted too much in expenses.

CM J. Brown asked about a way to estimate the amount of money the city will receive based on filed tax extensions. Cook said no but explained his concerns because of the variety of reasons that may cause extensions to be down; he said the goal is to process all tax returns filed by April 15 by early May.

Bledsoe expressed frustration with the variances that the city sees month to month while pointing out themes in the budget and the downward trends in revenue. She questioned if there is a better way to handle forecasting or see the trends beneath the numbers so we can understand it more clearly. Bledsoe eluded to a discussion about a two-year budget cycle and a potential partnership with UK to look at greater trend data.

<u>No further comment or action was taken on this item.</u>

March 2019 MTD Actual Compared to Adopted Budget:

Revenue Category	Actual	Budget	Variance	%Var
OLT- Employee Withholding	15,668,761	15,549,947	118,814	0.8%
OLT - Net Profit	4,402,058	4,227,318	174,740	4.1%
Insurance	1,128,221	61,407	1,066,814	1737.3%
Franchise Fees	2,730,001	2,359,856	370,145	15.7%
TOTALS	23,929,041	22,198,528	1,730,513	7.8%

March 2019 YTD Actual Compared to Adopted Budget:

Revenue Category	Actual	Budget	Variance	% Var
OLT- Employee Withholding	151,273,747	154,285,682	(3,011,935)	-2.0%
OLT - Net Profit	18,614,700	20,990,973	(2,376,273)	-11.3%
Insurance	25,167,284	24,703,861	463,423	1.9%
Franchise Fees	18,446,600	19,914,452	(1,467,852)	-7.4%
TOTALS	213,502,331	219,894,968	(6,392,637)	-2.9%

2019 Fiscal Year – Cash Flow Variance Revenue (Actual to Budget):

For the nine months ended March 31, 2019	Actuals	Budget	Variance	% Var
Revenue				
Payroll Withholding	151,273,747	154,285,682	(3,011,935)	-2.0%
Net Profit	18,614,700	20,990,973	(2,376,273)	-11.3%
Insurance	25,167,284	24,703,861	463,423	1.9%
Franchise Fees	18,446,600	19,914,452	(1,467,852)	-7.4%
Other Licenses & Permits	4,655,979	4,236,515	419,464	9.9%
Property Tax Accounts	23,773,491	23,856,651	(83,160)	-0.3%
Services	17,866,782	17,517,412	349,370	2.0%
Fines and Forfeitures	190,324	179,250	11,074	6.2%
Intergovernmental Revenue	269,848	305,347	(35,499)	-11.6%
Property Sales	171,128	187,500	(16,372)	-8.7%
Investment Income	1,098,801	351,753	747,048	212.4%
Other Financing Sources	1,284,712	1,194,000	90,712	7.6%
Other Income	2,788,082	2,597,027	191,055	7.4%
Total Revenues	**$265,601,480**	**$270,320,423**	**($4,718,943)**	**-1.7%**

2019 Fiscal Year – Cash Flow Variance Expense (Actual to Budget):

For the nine months ended March 31, 2019	Actuals	Budget	Variance	% Var
Expense				
Personnel	166,975,881	169,680,147	2,704,267	1.6%
Operating	34,812,043	42,329,285	7,517,242	17.8%
Insurance Expense	8,287,582	9,652,662	1,365,080	14.1%
Debt Service	34,213,964	36,197,150	1,983,187	5.5%
Partner Agencies	15,960,179	16,418,633	458,454	2.8%
Capital	412,609	1,352,395	939,786	69.5%
Total Expenses	**$260,662,257**	**$275,630,272**	**$14,968,016**	**5.4%**
Transfers	**3,799,910**	**2,900,627**	**(899,284)**	**107.5%**
Change in Fund Balance	**$1,139,312**	**($8,210,476)**	**$9,349,788**	

Comparison of Economic Indicators 2017/2018/2019:

Economic Indicators		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Fayette County	2017	4.0%	3.9%	3.9%	3.6%	3.6%	4.4%	4.5%	3.9%	3.2%	3.2%	3.1%	2.8%
Unemployment Rate	2018	3.0%	3.6%	3.4%	3.0%	3.2%	4.0%	3.8%	3.2%	3.2%	3.3%	2.7%	2.8%
	2019	3.3%	3.2%	N/A									
Quarterly Fayette County	2017	-	-	192,217	-	-	194,097	-	-	196,127	-	-	199,897
Employment	2018	-	-	191,578	-	-	193,808	-	-	194,500	-	-	N/A
	2019	-	-	N/A	-	-	N/A	-	-	N/A	-	-	N/A
Fayette County Permits Issued	2017	876	739	924	899	1,357	995	1,207	1,283	1,054	1,053	994	965
	2018	914	927	979	993	1,547	1,432	1,260	1,187	999	1,243	952	760
	2019	1,017	846	986									
Fayette County New Business	2017	201	253	418	468	621	328	206	281	205	247	213	140
Business Licenses	2018	219	250	379	751	535	286	166	264	209	279	174	149
	2019	216	259	446									
Home Sales (MSA)	2017	776	794	1,060	1,067	1,411	1,428	1,353	1,311	1,084	1,115	951	1,000
	2018	728	700	1,042	1,085	1,281	1,380	1,294	1,339	1,010	1,086	953	887
	2019	619	805	N/A									
Fayette County	2017	27	17	16	19	16	17	20	22	19	16	26	16
Foreclosures	2018	21	0	22	21	21	22	16	25	28	14	0	15
	2019	11	16	14									

N/A indicates information not available.
BLS Release Dates for Fayette Co. Quarterly Employment - 6 months after quarter end

FY19 Code Enforcement Nuisance Abatement/Lien Collections:

Month	Administrative Collection Fees		Miscellaneous		Penalty & Interest		Total Collections	
	FY 2019	FY 2018	FY 2019	FY 2018	FY 2019	FY 2018	FY 2019	FY 2018
July	675	825	1,430	603	15,407	6,936	17,512	8,364
August	75	1,125	2,068	1,711	61,651	35,892	63,794	38,728
September	225	800	4,083	1,260	31,372	55,540	35,680	57,600
October	150	375	2,431	536	88,286	50,654	90,867	51,565
November	225	525	1,247	1,664	28,552	40,359	30,024	42,548
December	375	600	1,548	572	33,737	31,407	35,660	32,579
January	150	424	2,138	1,832	43,646	56,185	45,934	58,441
February	600	225	2,476	1,170	54,389	61,030	57,465	62,425
March	450	525	5,153	969	75,355	61,448	80,958	62,942
Totals	2,925	5,424	22,576	10,317	432,393	399,451	457,894	415,192

III. Economic Outlook for 2019, Kentucky and Beyond

Dr. Jenny Minier, UK Professor of Economics and Director of the Center for Business and Economic Research, first explained the difference about the data they present between Fayette County and the Lexington metropolitan statistical area (MSA), which includes five surrounding counties. She reviewed general conditions of the national economy, comparing real GDP for the U.S. and Kentucky. She pointed out 16 percent growth in employment for Lexington MSA between December 2009 and March 2019 and highlighted the top employment sectors for the area; noting how agriculture is reported in the data because it is not measured by employers like other sectors. She talked about slow wage growth despite historically low unemployment rates, potentially caused by discouraged workers camouflaged in unemployment figures but who are actually available. She discussed household income in Fayette County, after showing a map of Kentucky's household income. Her forecast is that the economy will remain fairly strong but it will slow down; GDP growth has been fast and it will likely slow to a more moderate pace. Minier pointed out things that influence the economy such as trade policies and federal tax cuts that were made last year. She concluded her presentation highlighting pressing concerns for Lexington, such as pension funding and balancing growth with infill but pointed out strong fundamentals like high levels of education and relatively low cost of living.

CM Ellinger compared the strong economy and low unemployment rates to local constraints on revenue and the reason being tied to wage growth. Minier explained that slow wage growth is a significant contributor because they would expect wage growth to be higher; she described it as a national phenomenon.

J. Brown asked about the economic rationalization of the national tax cuts. Minier said it was supposed to increase investment and explained investment was initially high but it has trailed off. She added that using tax cuts to stimulate the economy is an old tradition that has been successful; though, the strategy is traditionally used when the economy is bad. They discussed the difficulties in measuring the agriculture employment sector because of its many affiliated jobs; the report UK produces on the industry was also mentioned.

CM Mossotti asked about any correlation between increasing the minimum wage and unemployment rates. Minier explained the direct impact is hard to tease out and that studies have found a variety of results. She pointed out differentiating factors such as raising the minimum wage statewide versus in a community, as well as the size of the increase compared to the actual local wages.

Moloney talked about the negative impact of the state's pension on Lexington, potentially causing the other Kentucky communities to go bankrupt. He also pointed out the impact of the city bonding at a 12-percent rate over the last few years versus the city's 10 percent target as outlined in LFUCG's Comprehensive Debt Management Policy. Moloney shifted to agriculture and said products like hemp provide a good outlook for Lexington and Kentucky and Minier added that a lot of jobs related to hemp won't only be in agriculture.

CM Evans asked to what level do you associate jobs with employment sectors. Minier explained one data set is self-reported from the worker versus other data that is reported by the employer. Evans asked about ways to calculate the average salary within the sectors, particularly for those who are working but still have difficulty affording to live in Lexington. Minier explained all sectors have a range of salaries so the average depends on the ratio of salary levels in each sector. CM Lamb references the data Minier presented on employment by sector and asked if it's possible to identify foreign-born workers. Minier said they might be able to find this information but they have not pulled it specifically.

Dr. Mike Clark, UK Associate Professor of Economics in the Gatton College of Business and Economics, talked about forecasts CBER has provided LFUCG regarding the occupational license tax in recent years, which includes forecasts of payroll revenue and net profit revenue. He pointed out the correlation between national trends and local trends, which helps identify patterns in our local data. He first talked about payroll tax for Lexington MSA, which trends very similarly to the U.S. He pointed out the decline of the employment growth rate, which falls below the national growth rate in 2018. While looking at covered employment, as reported by the Unemployment Insurance Program, he pointed out Lexington's employment level that started to fall in 2018. He said Lexington is seeing some wage growth but there is a decline in employment meaning fewer workers while total wages have been higher. Based on the same quarter in the previous year for FY19 payroll tax revenue projections, he presented a low forecast of 4.4 percent growth and high forecast of 5.4 percent growth, which is based on the most up to date data that reflects on Lexington's current economy. He concluded his presentation with net profit projections seeing a decline of 6.9 percent in FY19 and 8.7 percent growth in FY20.

Kay asked about the projected growth for net profit tax revenue in FY20, which Clark explained the typical pattern bounces around. CM Farmer asked Minier to send the median household income map from her presentation. He talked about the weight of retail in Lexington and the impact on the payroll tax. Clark said we have fewer people working in Lexington and that wages are up but not as high as they previously had been. He also pointed out this does not fully reflect the entire tax base because it's based on unemployment insurance. He highlighted growth on the national, state and MSA levels and said the slowdown is somewhat unprecedented. He added they have not done an analysis on which employment sectors are seeing less growth. They discussed the need to draw out the trends.

Lamb asked about the percent of change for Lexington employment. Clark explained that this information compares current-year month to prior-year month. She talked about other potential revenue sources that surrounding counties may use that could benefit Lexington, which is impacted by the state. Clark referenced a state task force he was part of in the early 2000s that resulted in a report regarding local sales tax, which probably remains a good resource despite its age.

Evans talked about industries that may be in turmoil and how that factors into the data Clark presented. Clark reviewed how the data is collected quarterly from employers, which is essentially an account of the workers in Lexington. He explained that the slowdown is likely coming from multiple sectors and that they will continue to drill down into that data. Bledsoe asked about Lexington MSA remaining fairly stable while Lexington experiences slower growth and whether there is a migration happening to the surrounding counties. Clark said it may be hard to get to that data but they can look into it.

Moloney talked about baby boomers retiring, particularly for LFUCG and UK, and employers not filling those positions, therefore impacting the economy. Clark said it is possible but they cannot track individuals on the local level and it would probably require a lot more data about people on a five-year estimate. Moloney said 51 percent of the people who work in Lexington live outside of the county. He asked about the possible need to increase taxes and if that point is approaching. Clark explained tax policy decisions need to be made based on the services that are provided to and needed by Lexington residents.

Farmer talked about the city's relationship with UK and their expertise with forecasting. Cook explained the existing exchange of information between the entities and the intent to grow the already strong relationship.

Kay said the unemployment rate is a less valuable assessment of the health of our economy, instead, we should be looking at the employment level. Clark explained that unemployment is a good long-term status of the economy. He cited the example of discouraged workers after the recession (e.g. individuals who left the labor force and therefore were not tracked as unemployed) and emphasized the fact that there are fewer people in the labor force. He said the number of people working is a more accurate indication of what is going on. Kay talked about the spike in Lexington's employment in late 2017 and then a drop in early 2018. He concluded the change over time is headed in the right direction and that the actual numbers may be more helpful than the percent of change. He asked what happened in 2017. Cook pointed out a yearly trend for Lexington employment to increase towards December, drop in January and then begin to climb back up; a similar trend is reflected in the unemployment rate. They agreed 2018 fourth-quarter employment will likely go up from the third quarter.

Plomin talked about the recently completed housing study, which identified 52 percent of people that work in Lexington commute from surrounding counties, and the benefitting impact that has on Lexington. Clark said you might be surprised how far some people travel to work in Lexington and that Lexington is a net importer of labor. He explained there are some costs associated with them working in Lexington, such as police and fire protection and sanitary sewer but you don't have the residential costs.

<u>No further comment or action was taken on this item.</u>

IV. Items Referred to Committee

<u>No comment or action was taken on this item.</u>

<u>A motion was made by CM Evans to adjourn at 2:54 p.m., seconded by CM Ellinger. The motion passed without dissent.</u>

H.A. 8/6/19