CITY MANAGER'S BUDGET MESSAGE

April 1, 2020

The Honorable Mayor and Assembly
City and Borough of Juneau
Juneau, Alaska

CITY MANAGER'S BUDGET MESSAGE

In accordance with the Municipal Charter, attached is the balanced FY21 and FY22 Operating and Capital Budgets. In it, I am recommending that you begin the budget process with the assumption of a property tax increase of 1 mil, nearly 10%.

With no exaggeration, these are unprecedented times. I recommend that the Assembly bring this recommendation through the public budget process and make a final decision that is informed by the following factors:

1. Forecast impact to our local economy resulting from the global COVID-19 pandemic.
2. Updated estimate of shortfalls in collection of sales tax in the current and future years.
3. Updated accounting of expenses incurred due to COVID-19 mitigation.
4. Assembly consideration of Manager's recommendation on the Capital Improvement Plan.
5. Whether or not the State of Alaska fully funds School Bond Debt Reimbursement.
6. Service Reductions as specifically targeted or a dollar amount as requested by the Assembly.
7. The amount of State or Federal financial relief that becomes available, if any.

Given the unprecedented level of uncertainty, you may wish to think of this budget as an "interim," "draft," or "placeholder" budget with the intention to return to a formal budget process once the dust has settled from the public health crisis we are now experiencing. That work will certainly need to happen in the fall of 2020 or the winter of 2021. However, be advised that the Charter 9.7 (a) requires you to pass a budget by June 15, or the Manager's budget shall be deemed adopted. We must work hard together to ensure that the Assembly is able to pass a budget.

The budget process began with the Assembly's direction to the Manager in early December. I conveyed that direction to the Departments in mid-December and they created their budgets in January. The Manager's Office and Finance Department reviewed those budgets extensively in February in consultation with Directors and key administrative staff. The budget presented here was largely complete by March 1st—significantly before we understood the scope and scale of the spread of COVID-19 and its potential impact on Juneau's community and economy.

This budget reflects revised projections of consumer tax revenues and passenger fees in light of COVID-19. However, it does *not* reflect the impact of COVID-19 on any of the following:

- Departmental Expenditures
- User Fees and Charges for Services
- Enterprise Budgets (expenditure or revenue)
- Capital Improvement Plan

CITY MANAGER'S BUDGET MESSAGE

This budget assumes no cruise ship season in the summer of 2020, and it assumes a tepid season in 2021. Note that the impact of lost cruise ship seasons will be felt across two fiscal years, between FY2020 and FY2021 for this summer's season and across FY2021 and FY2022 for next summer's season. This budget also assumes that the shelter-in-place mandates persist through at least July 1st. This budget also assumes that contraction in the national US economy will result in higher unemployment and less disposable income for several years into the future. These assumptions combined have a severe impact on Sales Tax, Hotel-Bed Tax, other consumer taxes, and all passenger fees. This budget assumes that the State of Alaska will only reimburse 50% of its portion of School Bond Debt in FY2020, FY2021, and FY2022—which is proposed to be fully paid from the Debt Service Fund. One area of stability: this budget projects that property taxes will remain stable after a 1% increase in property valuation in FY2021. At this time, it would be foolish to speculate about the future erosion of property values as a result of the COVID-19 pandemic.

During the budget process, we will discuss the sizable depletion of unrestricted fund balance and the restricted budget reserve over the next two fiscal years. To offset this substantial decline in available funds, I have proposed a 1.0 mill increase to the areawide rate that will generate approximately $5.0 million in each of FY2021 and FY2022. Without that proposed increase, by the end of FY2022, this budget could fully drain both the unrestricted fund balance and the restricted budget reserve.

The Assembly has big levers to pull-on to change the trajectory of the budget and resulting fund balances. One option would be to reduce the historic level of investment in capital projects. The FY2021 and FY2022 Capital Improvement Plans will each fund approximately $20 million of projects with general government and sales tax funds. Even a modest reduction of these substantial infrastructure investments can move the needle. Further, the Assembly can work with the Manager to review existing appropriations for capital improvement projects. Not all projects move at the same speed, and there may be projects that have stalled. There may also be already-appropriated projects that the Assembly no longer views as critical community priorities. De-appropriating these projects can effectively add those funds back to fund balance. Lastly, the Assembly can consider reduction of CBJ operations. To do so, the Assembly can return to the Program Prioritization work that it completed in 2019 where it identified programs as higher or lower priority.

SUMMARY

This City Manager's Budget Message is the shortest in a very long time. You may find that merciful, or you may find yourself wanting more of the ugly detail. We will get to the ugly detail for sure. However, I think the Assembly can do itself a favor by recognizing that the coming year's budget will be a work-in-progress well into next fall. For now, I encourage you to wrestle with the big concepts but avoid becoming lost in the uncertainty in the margins. Again, we live in unprecedented times.

I appreciate the hard work put in by the CBJ staff to prepare this year's budget for introduction. In spite of the uncertainty created by our current public health emergency, this budget reflects significant efforts by CBJ staff to retain status quo expenditures while sustaining critical municipal services. Additionally, I appreciate the work CBJ employees have undertaken over the past years to reduce expenditures and be wise consumers.

Respectfully submitted,

Duncan Rorie Watt
City and Borough Manager

MEMORANDUM

DATE: April 1, 2020

TO: Assembly Finance Committee

FROM: Jeff Rogers, Finance Director

SUBJECT: FY21/22 Revenue Overview

155 Municipal Way
Juneau, AK 99801
Phone: (907) 586-5215
Fax: (907) 586-0358

Background

As has been said by the Manager, we live in unprecedented times. There is an uncomfortable balance between rationale analysis and pure speculation. The revenues forecast in the proposed budget are generally up-to-date with current understanding of the COVID-19 pandemic and the ensuing impact on the global, national, and local economies. These revenue forecasts generally assume the following:

- No 2020 cruise ship season
- 2021 cruise ship season is tepid (roughly 2018 level)
- Government-mandated shelter-in-place continues through June, but eases thereafter
- Mid-term national recessionary environment

In no way do these assumptions suggest that these are or will be the policies of the CBJ. However, these assumptions likely represent a mean case that is neither too optimistic nor too conservative. See attached revenue tables.

Sales Tax

Reduced sales tax receipts will be the most significant budget impact from COVID-19. From the peak of $50.4 in FY2019, $43.0 million and $41.7 million are forecast respectively for FY2020 and FY2021. Note that the impact of the lost summer cruise season is split between two fiscal years. The last quarter of FY2020 (the quarter beginning April 1 2020) is forecast to be just $7.0 million in sales tax, which is less than half the amount of tax received in that same quarter in the prior year. This quarter is also forecast to be the “eye of the needle” after which sales tax will begin to normalize, though not very quickly. The first quarter of FY2021 (the quarter beginning July 1 2020) is forecast to be $10.9 million, a decline from $17.1 million in the previous year. This forecast amount assumes that shelter-in-place orders are no longer in effect and that the economy has started to normalize. Forecasts for the quarters starting October 1 2020 and January 1 2021 reflect modest contraction from prior years. And the forecasts for the quarters beginning April 1 2021 and July 1 2021 reflect a full (though not robust) cruise ship and visitor season. As a small offset to these forecast reductions, Remote Sales Tax is forecast at $0.2 million in FY2020, $1.2 million in FY2021, and $1.5 million in FY2022. These forecasts are unadjusted from previous forecasts for remote sales tax.

Using actual FY2019 sales taxes as the base line, these sales tax forecasts represent almost $18 million in lost sales taxes over roughly two years as a result of impacts from the COVID-19 epidemic—$7.4 million in FY2020, $8.7 million in FY2021, and $1.8 in FY2022. If compared to previous forecasts that anticipated sales tax growth, the lost revenue would be even greater.

Minor Consumer Taxes

Forecasting hotel-bed tax is challenging in this environment. As of this memo, the Four Points Sheraton has closed to business. The Baranof appears to be open, though it has many long-term rentals to the legislature that are not subject to hotel-bed tax. The decline in cruise ship tourism has an impact on hotel bed tax but it is not linear because only a small fraction of cruise visitors stay overnight in Juneau. Anecdotally, we know that some individuals are using hotels for the purpose of self-isolation, either from their local families or as part of state-mandated travel quarantines. From a high of $1.64 million in FY2019, hotel-bed taxes are forecast to be $1.35 million in FY2020, $0.81 million in FY2021, and then rebounding to $1.44 million in FY2022. The Assembly will face decisions about the level of funding to be offered to Travel Juneau and Centennial Hall.

Liquor taxes will be significantly impacted by the closure of bars and restaurants, though it would be reasonable to assume that package sales have risen commensurately. The lack of a summer tourism season likely reduces total consumption considerably. From a high of $1.02 million FY2019, liquor taxes are forecast to be $0.86 million in FY2020, $0.73 million in FY2021, and then rebounding to $0.89 million in FY2022. The forecast takes a similarly conservative view of marijuana taxes, but since marijuana dispensaries have remained open as critical business, these forecast estimates may unnecessarily conservative. From a high of $0.28 million in FY2019, marijuana taxes are forecast to be $0.25 million in FY2020, $0.20 million in FY2021, and then rebounding to $0.25 million in FY2022. Anecdotally, retail marijuana sales have remained strong during the shelter-in-place mandate.

Tobacco taxes are likely the least responsive to local shelter-in-place orders, but the absence of summer tourism will reduce the overall consumption volume. From a high of $2.9 million in FY2019, tobacco taxes are forecast to be $2.7 million in FY2020, $2.4 million in FY2021, and then rebounding to $2.7 million in FY2022.

<u>Passenger Fees</u>

Considering all three of the applicable passenger fees together, from a high of $14.7 million in FY2019, passenger fees are forecast to be $14.5 million in FY2020, $6.7 million in FY2021, and then rebounding to $10.4 million in FY2022. That trend is unusual, for a number of reasons. Most significantly, state Commercial Passenger Vessel fees are remitted to CBJ once per year in the fall *after* the prior fiscal year has concluded, and CBJ records those remitted fees in that fiscal year. So, for the current year, FY2020, CBJ has already received all of its budgeted state CPV fee revenue from the state. On top of that, supplemental state legislation includes $2.4 million of additional CPV revenue to be paid in the current year. Hence, even though CBJ will not receive passenger fees for the remainder of the current year, FY2020 total passenger fees are largely unaffected by COVID.

However, this lagging factor of CPV will dampen the longer-term trend of passenger fees. In this regard, FY2021 is the “eye of the needle” with just $6.7 million in passenger fees to be received, which reflects small amounts to be received in last quarter during the summer 2021 cruise season as well as the delayed payment of CPV from the State from the prior year. FY2022 would otherwise be a more normalized year, but the delay of CPV catches up and reduces total passenger fees in that year also.

CBJ’s advantage with passenger fees is that they primarily fund capital improvements that can simply delayed until fees are available. Each year, CBJ must pay debt services of approximately $2.1 million on the 16B docks. Additionally, CBJ experienced approximately $2.5 million of costs for city services related to the summer cruise season. Note: while the 2020 cruise season is not forecast to happen, CBJ cannot ramp down its capacity for general city services for that limited period—these are ongoing sunk costs in overall CBJ capacity.

<u>Property Tax</u>

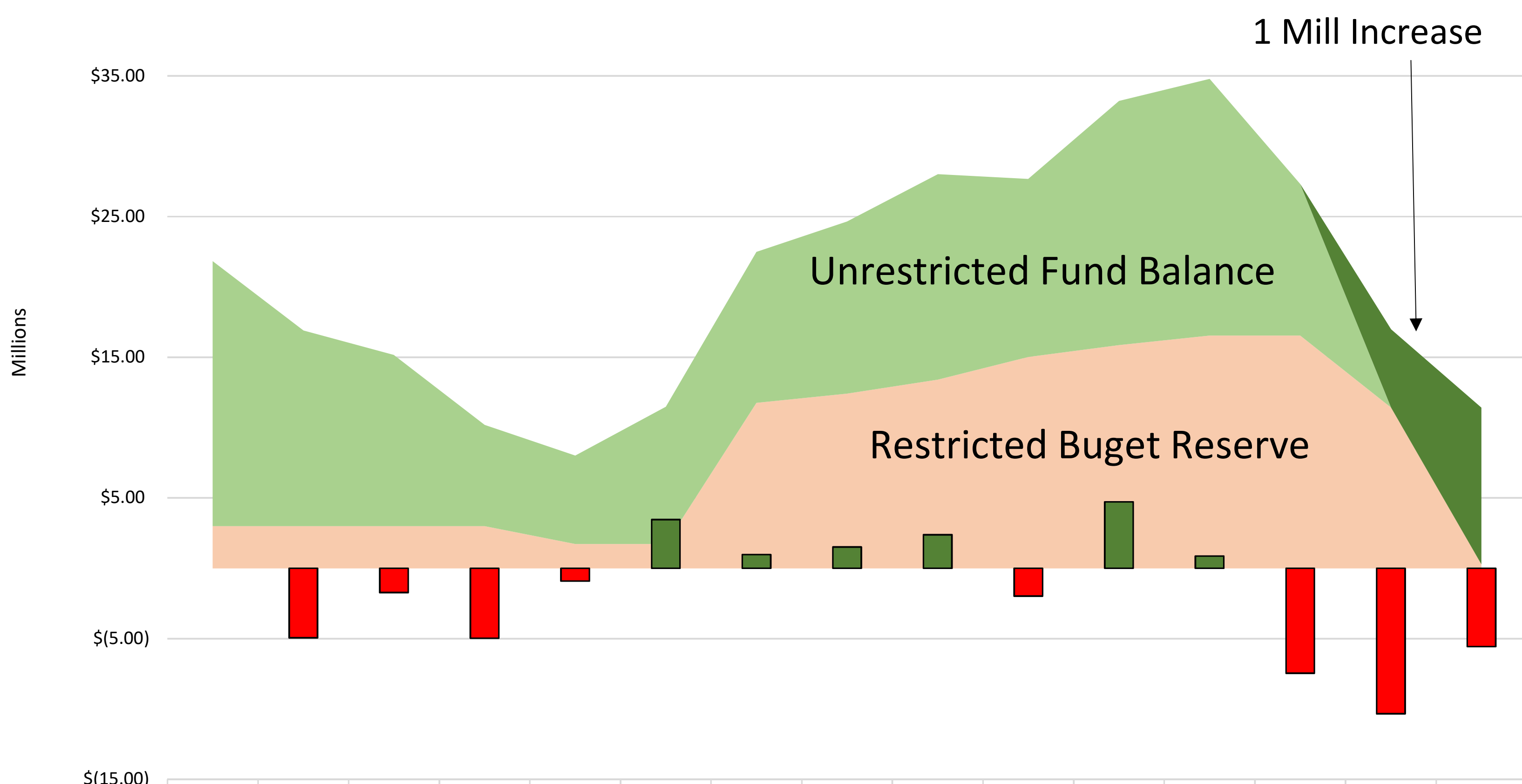
Property tax is not forecast in the same way as other consumer taxes. Importantly, property tax revenue is a factor of only two things: assessed valuation and the mill rate. Assessed valuations are always determined on January 1 for the tax revenue generated in the next fiscal year. So, FY2021 property tax revenues are dependent on valuations from January 1 2020—before the COVID pandemic had spread. Assessment cards were mailed on March 27 2020, and the process of appeals has begun. Based on the assessments and anticipated appeals, we expect valuations will have risen by approximately 1.4% to $5.07 billion. Naturally, property tax receipts would increase by that same factor. However, the Proposed budget includes a 1.0 mill increase to the rate, which would generate an additional $5.1 million in each of FY2021 and FY2022.

<u>Conclusion</u>

Consideration of the Proposed FY2021/FY2022 Budget is likely to center significantly on revenue estimates and the impact on fund and reserve balances. The Finance Department is prepared to update these revenue forecasts mid-cycle if new circumstance indicate that updates are warranted.

15-Year Operating Fund Balance History and Projections
With Proposed 1.0 Mill Property Tax Increase

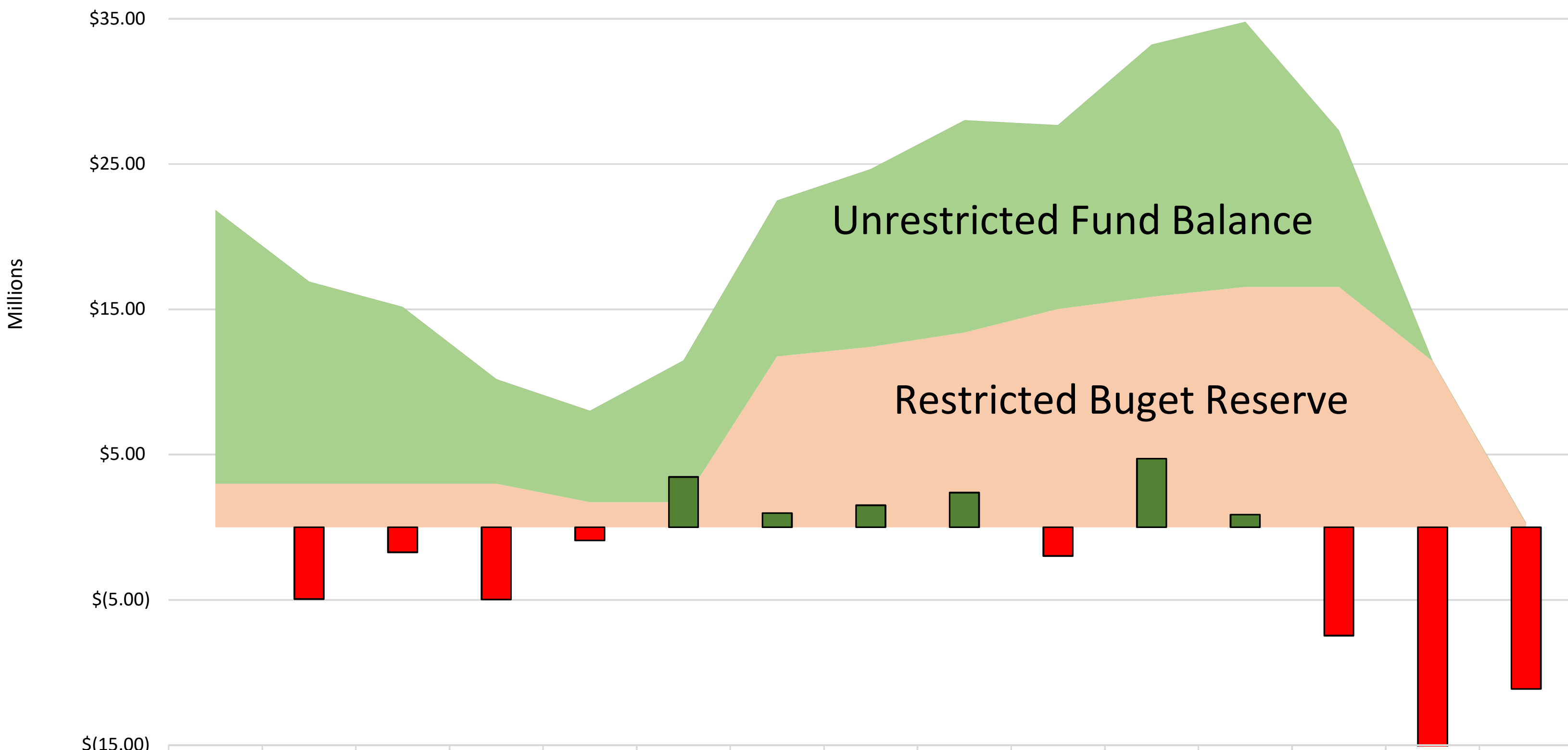
Updated 3/30/2020



	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016	FY2017	FY2018	FY2019	FY2020	FY2021	FY2022
One Mill PT Increase (cumulative)														$5.56	$11.12
Unrestricted Fund Balance	$18.84	$13.90	$12.17	$7.20	$6.29	$9.75	$10.72	$12.23	$14.62	$12.64	$17.37	$18.23	$10.77	$-	$-
Reserves	$3.00	$3.00	$3.00	$3.00	$1.73	$1.73	$11.76	$12.41	$13.41	$15.02	$15.86	$16.55	$16.55	$11.42	$0.29
Surplus/(Deficit)		$(4.94)	$(1.72)	$(4.97)	$(0.91)	$3.46	$0.97	$1.51	$2.39	$(1.98)	$4.72	$0.86	$(7.46)	$(10.34)	$(5.57)

15-Year Operating Fund Balance History and Projections
Without Proposed 1.0 Mill Property Tax Increase

Updated 3/30/2020



	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016	FY2017	FY2018	FY2019	FY2020	FY2021	FY2022
One Mill PT Increase (cumulative)															
Unrestricted Fund Balance	$18.84	$13.90	$12.17	$7.20	$6.29	$9.75	$10.72	$12.23	$14.62	$12.64	$17.37	$18.23	$10.77	$-	$-
Reserves	$3.00	$3.00	$3.00	$3.00	$1.73	$1.73	$11.76	$12.41	$13.41	$15.02	$15.86	$16.55	$16.55	$11.42	$0.29
Surplus/(Deficit)		$(4.94)	$(1.72)	$(4.97)	$(0.91)	$3.46	$0.97	$1.51	$2.39	$(1.98)	$4.72	$0.86	$(7.46)	$(15.90)	$(11.13)