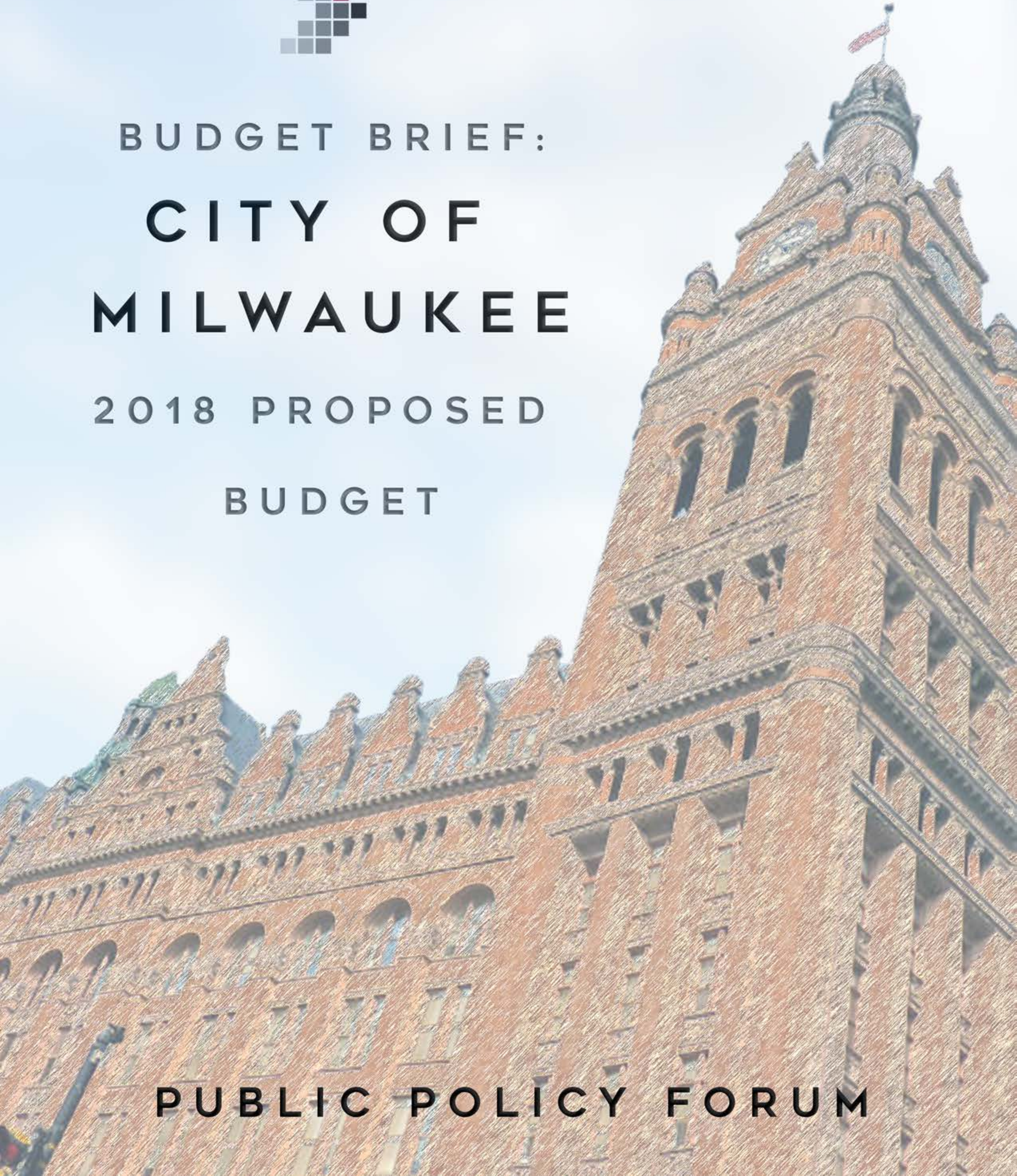
BUDGET BRIEF:

CITY OF MILWAUKEE

2018 PROPOSED BUDGET



PUBLIC POLICY FORUM

ABOUT THE PUBLIC POLICY FORUM

The Milwaukee-based Public Policy Forum, established in 1913 as a local government watchdog, is a nonpartisan, nonprofit organization dedicated to enhancing the effectiveness of government and the development of Southeastern Wisconsin through objective research of regional public policy issues.

PREFACE AND ACKNOWLEDGMENTS

This report is intended to provide citizens and policymakers with an independent, comprehensive, and objective analysis of the Mayor's proposed City of Milwaukee budget. We hope that policymakers and community leaders will use the report's findings to inform discussions during upcoming budget deliberations.

Report authors would like to thank Milwaukee fiscal officials and staff – including the Budget Director and his staff – for their assistance in providing information on the City's finances.

Finally, we wish to thank the Northwestern Mutual Foundation for generously supporting our local government finance research.

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2018 Proposed City of Milwaukee Budget

OCTOBER 2017

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INTRODUCTION

In the concluding paragraph of *On the Money?*, our July 2017 report on the City of Milwaukee's revenue structure, we warned that the City's ability to pay for "core municipal services" would come under "increasing duress" without modification to the existing structure. The Mayor's proposed budget for 2018 provides definition to that warning.

The City's structural imbalance – caused by the conflict between stagnant revenue streams and fierce personnel-related expenditure pressures – is relatively old news. This budget, however, marks the first since 2010 in which the Milwaukee Police Department (MPD) is not shielded from deficit reduction strategies that have been commonplace for most other City departments. In the absence of this special treatment, 33 positions would be cut from MPD and an additional 75 would be cut from the Milwaukee Fire Department (MFD), the two departments in City government whose services many would consider to be its most "core."

In addition to signaling a conclusion that *all* departments now must share relatively equally in the City's annual quest for savings, this decision also reflects the severity of the City's financial challenges for 2018. The primary culprit is a spike in the employer pension contribution, which increases from $61 million to $83 million, largely because of new actuarial assumptions. Also, the City must reduce its withdrawal from the Tax Stabilization Fund by more than $8 million, as its ability to replenish the Fund has not kept pace with recent draws.

On the revenue side, intergovernmental revenues again are flat, growing by only $1.8 million (0.7%) from the 2017 amount. To offset that lack of growth and respond to the increased pension payment, the budget proposes a $9.7 million (3.7%) increase in the property tax levy – the largest percentage increase since 2010. If that levy amount is adopted, then the property tax – for the first time – would replace intergovernmental revenue as the City's largest single revenue source.

While the three P's – public safety, pensions, and property taxes – are the main story lines of the 2018 proposed budget, there are other elements that should not go unnoticed. One is the unexpected $6.7 million reduction in health care spending, which provides badly needed cushion with which to partially offset the growth in pension costs, but which likely cannot be sustained in future years. Meanwhile, on the capital side, the budget includes a fiscally prudent decision to reduce levy-supported borrowing by $12.7 million, though this may generate concerns about the City's ability to appropriately meet its capital needs.

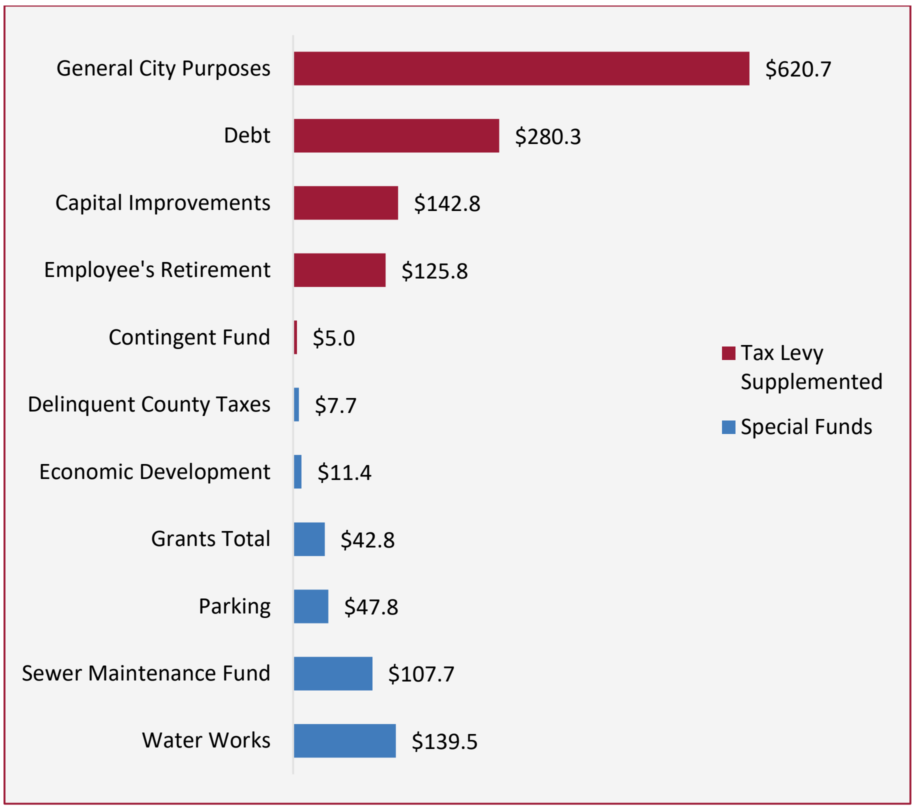
Overall, this is a watershed budget for the City. The Mayor's refusal to shield public safety represents a change in thinking – one that he contends only should be reversed if State lawmakers provide the City with the ability to implement a local sales tax. As the Common Council considers the budget, it will have to determine whether it agrees, or which difficult choices it would prefer as alternatives to public safety reductions.

In the pages that follow, we provide additional detail on important elements of the 2018 proposed budget, including discussion of five keys to understanding the budget. Our intent is to promote more informed discussion and debate as budget deliberations continue.

2018 PROPOSED BUDGET OVERVIEW

The City of Milwaukee's 2018 proposed budget totals a little over $1.5 billion, which is slightly ($2.5 million) lower than the 2017 adopted budget. The "property tax supplemented" portion of the budget refers to those components that receive at least partial support from the City's property tax levy and that generally are controlled by the Mayor and the Common Council. As shown in **Figure 1**, that portion totals about $1.2 billion. The City also has several special purpose funds (totaling $357 million) that have their own dedicated fees or other revenues to support specific functions, such as sewer, water, and parking.

Figure 1: Summary of 2018 Proposed Budget (in millions)



Property Tax Supplemented Budget

= $1.174 Billion

Total Special Funds

= $357.0 Million

Total 2018 Proposed Budget = $1.531 Billion

Source: City of Milwaukee budget documents[1]

In this brief, we focus most of our attention on the portions of the budget controlled by the Mayor and Common Council, with particular emphasis placed on the general city purposes budget. That portion of the budget – commonly known as the "general fund" – totals a little under $621 million in the 2018 proposed budget.

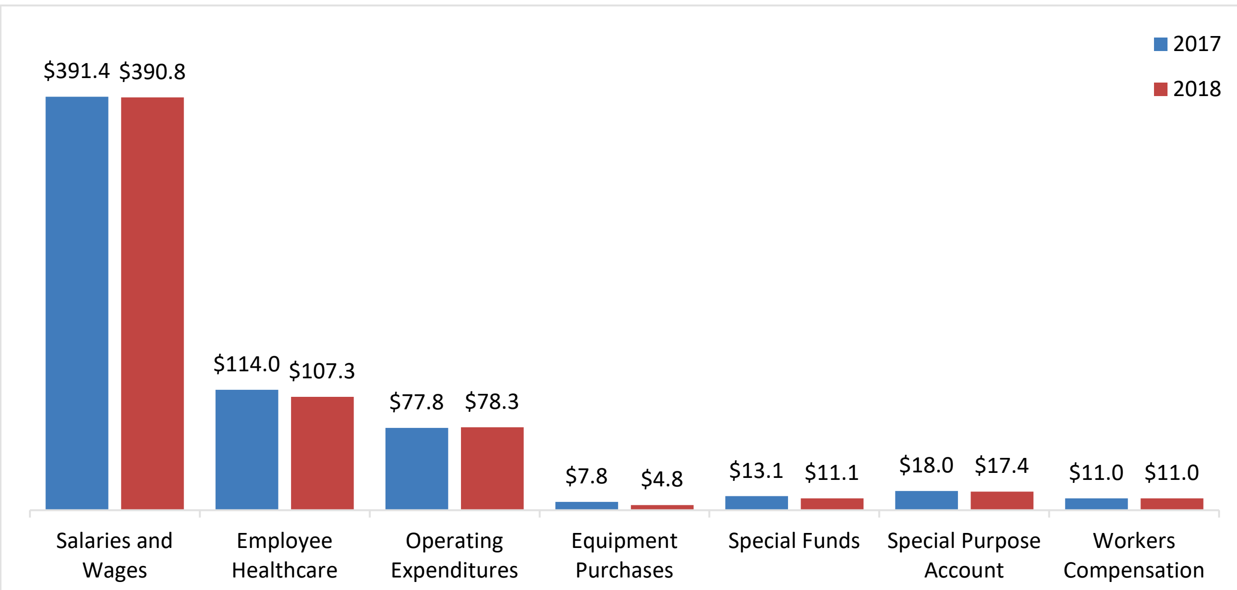
[1] Unless otherwise noted, the source for all figures, tables, and charts in this report is City of Milwaukee budget documents.

GENERAL CITY PURPOSE EXPENDITURES

The City's general purpose expenditures support many of the daily workings of City government, including some of its most visible functions like police, fire, public works, libraries, and public health. The $620.7 million allocated to general city purposes in the 2018 proposed budget is a decrease of $12.2 million (1.9%) from 2017. The decrease primarily is caused by the need to shift additional funds to the Employees Retirement Fund to accommodate the significant increase in the City's employer pension contribution, as will be discussed in greater detail below.

Chart 1 breaks down proposed 2018 general city purpose spending by expenditure type and compares 2017 adopted to 2018 proposed amounts. The chart shows that the overall decrease in general purpose expenditures includes a $6.7 million reduction in healthcare expenditures; a $3 million reduction in equipment purchases; and a $2 million reduction in special funds.[2] It also shows that personnel-related expenditures comprise, by far, the largest portion of general purpose expenditures, as Salaries and Wages, Employee Healthcare, and Workers Compensation together account for 82% of total expenditures.

Chart 1: General city purpose spending by expenditure type (In millions)



When we compare 2017 versus 2018 proposed general purpose spending in the City's nine largest departments, the large cuts to police and fire stand out. As shown In **Chart 2**, proposed expenditures for the Milwaukee Police Department (MPD) decline by $8.7 million (2.9%), while proposed expenditures for the Milwaukee Fire Department (MFD) fall by $10 million (8.2%). Other sizable decreases are observed in the Department of Public Works ($2.4 million or 1.9%); Library ($520,000 or 2.2%); and Department of Neighborhood Services ($808,000 or 4%). Overall, spending for these nine major departments declines by $23.9 million in the proposed budget.

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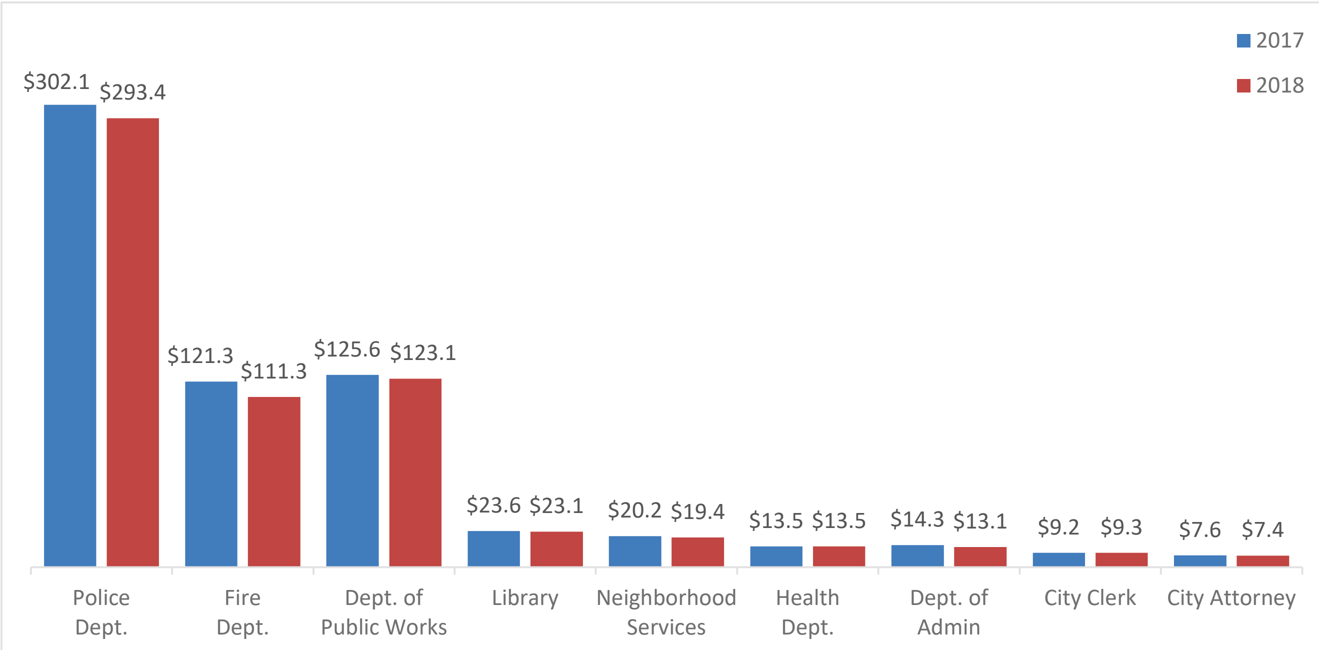
[2] It is important to note that wages and salaries remain relatively flat after a large increase in that category for Fire and Police in the 2017 budget.

Chart 2: General purpose spending in the City's nine largest departments (in millions)



GENERAL CITY PURPOSE REVENUES

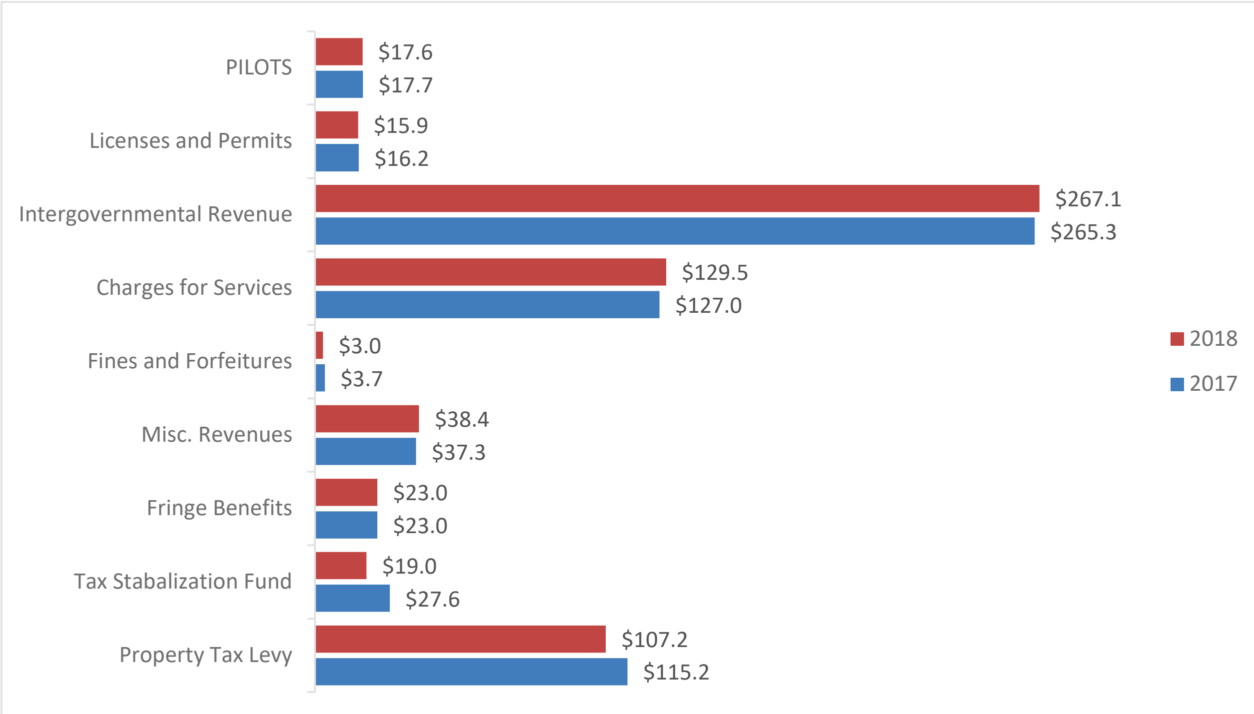
The City's general fund depends heavily on three major sources of revenue: Intergovernmental Revenue, Charges for Services, and Property Tax Levy. Together, these three revenue streams comprise more than 80% of proposed general city purpose revenues in 2018.[3]

Chart 3 – which compares 2017 adopted and 2018 proposed sources of general city purpose revenue – shows that the amount of property tax revenue allocated to the general fund would decline by $8 million (6.9%) in 2018, despite a proposed $9.7 million (3.7%) increase in the City's total levy, from $263.8 million to 273.5 million.[4] This reflects a need to increase by $16 million (21%) the amount of property tax levy directed to the Employees Retirement Fund to cover the increased employer pension contribution. Other portions of the property tax levy support Capital Improvements, City Debt, and the Common Council Contingent Fund.

[3] More in-depth analysis of the City's revenue structure can be found in our July 2017 report, *On the Money?*, at https://publicpolicyforum.org/research/money-city-milwaukees-uncommon-revenue-structure-and-how-it-compares-peer-cities.

[4] The proposed property tax rate in 2018 is $10.77, up from $10.75 in 2017.

Chart 3: Sources of general city purpose revenue (in millions)



The chart also shows that Charges for Services revenue for general city purposes would increase by $2.4 million (1.9%). Specific increases to major service charges are shown in **Table 1** and are consistent with previous projections by budget officials that major service fees will need to increase by 3-5% annually. We also see that Intergovernmental Revenue shows a slight increase of $1.8 million, or 0.7%; and that the $19 million contribution from the Tax Stabilization Fund is $8.6 million lower than the 2017 contribution of $27.6 million (we will discuss this matter in greater detail later in this report).

Table 1: Increases to major service charges

Charge for Service	Rate Increase	Cost Increase for Average Home
Solid waste fee	3%	$202.84 to $208.92 per year
Stormwater fee	3%	$80.72 to $83.16 per year
Snow and ice removal fee	3%	$37.72 to $38.85 per year

FIVE KEYS TO UNDERSTANDING THE 2018 BUDGET

LARGE SPIKE IN PENSION CONTRIBUTION MUST BE ACCOMMODATED

Prior to 2010, the City enjoyed 15 consecutive years in which it was not required to make an employer pension contribution because its pension fund was in an “overfunded” status. In that year, however, after the value of pension fund assets plummeted from the Great Recession, the City was required to come up with a $49 million contribution. A contribution again was not required in 2011 and 2012, but the City was required to make a nearly $60 million contribution in 2013. Since then, the required contribution has hovered around $60 million, with a $61 million contribution budgeted in 2017.

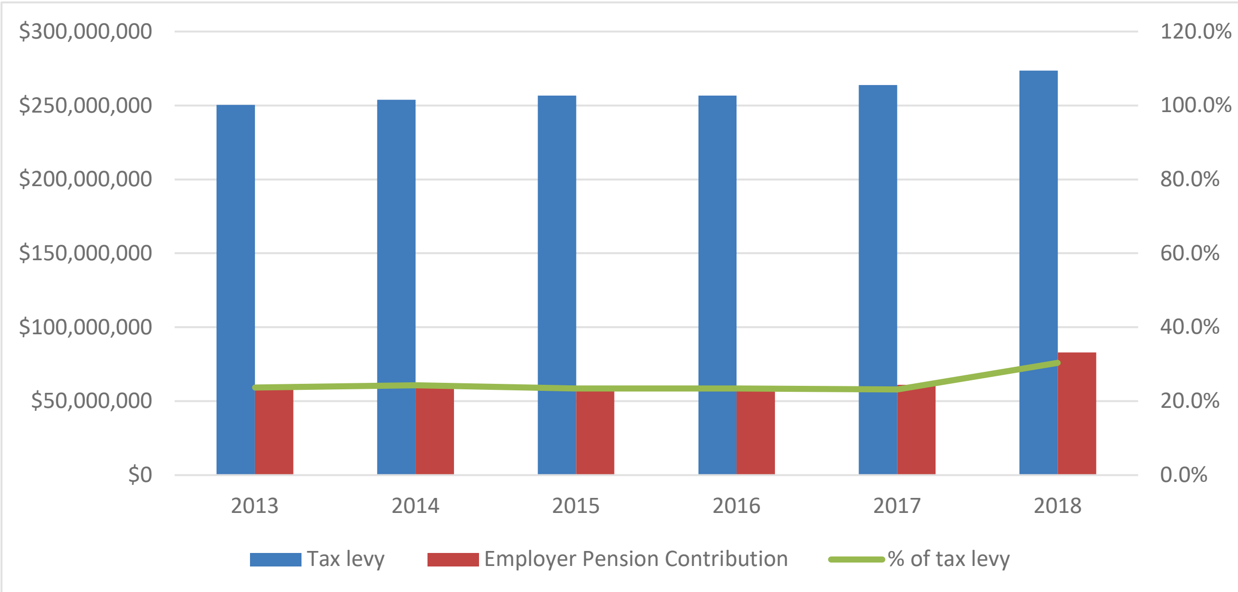
The City made an important change to address the volatility of annual contributions by adopting a stable contribution policy in 2013. Previously, the City Charter prohibited employer contributions to the fund when the plan was overfunded, which created the possibility of sharp swings in required contributions from one budget to the next (as occurred in both 2010 and 2013). The new policy requires the City to contribute an actuarially-determined amount based on a percentage of payroll. The contribution amount is set for a five-year period, after which it is reviewed and re-set for another five years. The new policy requires a contribution regardless of the plan's funded status.

A primary benefit to this approach is that City leaders can conduct budget planning with knowledge of the approximate scope of annual contributions at the beginning of each five-year period. Nevertheless, the size of the contribution still has been immense, and there now is a possibility that it will grow substantially by virtue of the re-setting process every five years.

That is precisely the case for 2018, as re-setting is occurring for the 2018-2022 timeframe. Because of new assumptions regarding the rate of return on fund investments (the assumed rate decreases from 8.25% to 8%) and other changes based on an experience study, the employer contribution jumps $22 million, from $61 million in 2017 to $83 million in 2018. It is expected to stay at about that level for the following four years.

As shown in **Chart 4**, the City’s employer contribution as a percentage of the property tax levy remained relatively steady because of the stable contribution policy from 2013 to 2017. In 2018, however, it would increase from 23.1% of the City’s total tax levy to 30.3%. This sharp jump obviously has an impact on the City’s wherewithal to support departmental operations, as well as its capacity to issue levy-supported debt for needed capital improvements.

Chart 4: Employer pension contributions and property tax levy, 2013-2018

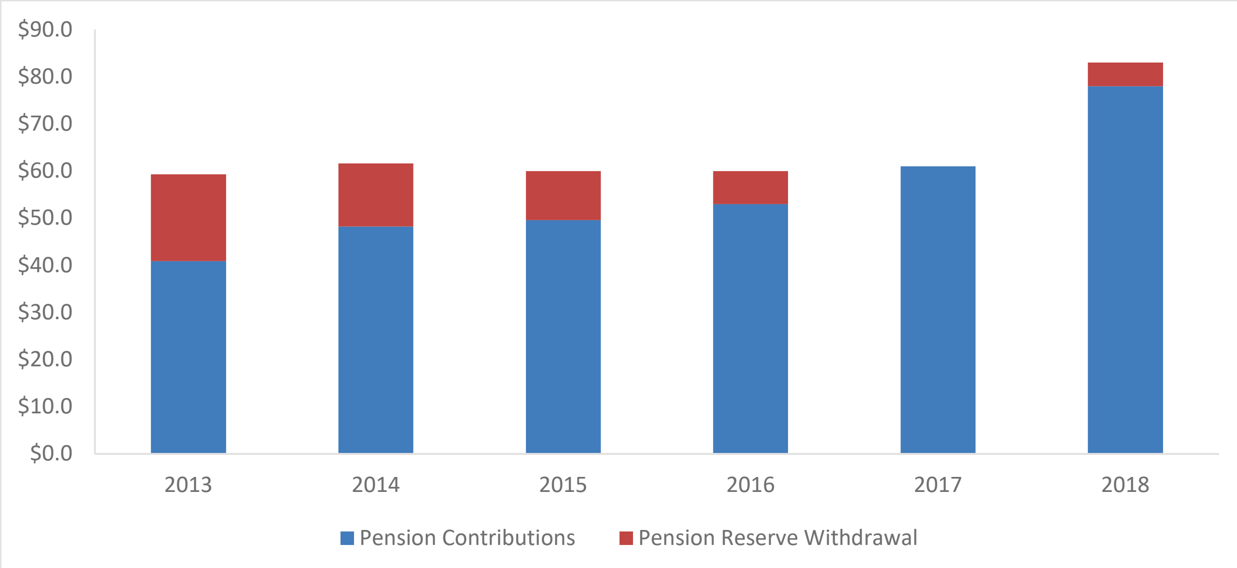


While the stable contribution policy benefits the City by providing predictability in the employer contribution for a five-year period, all volatility is not eliminated. In the proposed budget, $5 million of the $83 million contribution would come from a withdrawal from the pension reserve fund, while the remaining $78 million would come from the City's property tax levy. The proposed use of $5 million of reserves certainly is justified in light of the magnitude of the employer contribution increase, but the likely inability to match that draw from the reserve in future years will create the need for increased use of property tax levy in the intervening years.

The fact that the City has a relatively healthy pension reserve results from far-sighted decision-making by City leaders in 2011 and 2012. While no employer contribution was required in those years, City leaders instead wisely built the pension reserve, making $44 million of property tax levy contributions in those years. **Chart 5** (on the following page) shows that reserve funds then were withdrawn liberally – as would have been expected – to cushion the blow of the huge spike to $60 million in 2013 and in the years immediately following. Use of the reserve then diminished as its balance was spent down, and no reserve contribution was made in the 2017 budget.

As of the end of 2017, the pension reserve will contain $15.6 million. The proposed use of $5 million in 2018 would reduce it to $10.6 million, which means that continued use at that level only would be feasible for two more years. Even that level of usage is unlikely, however, as policymakers likely will want to leave some funding in the reserve to address a potential spike in 2023, when the next re-setting process occurs. Consequently, additional property tax levy is likely to be required to fill the gap as soon as 2019 and certainly in the years immediately following.

Chart 5: Employer pension contributions and pension reserve withdrawals, 2013-2018 (in millions)



PUBLIC SAFETY IS NOT SHIELDED FROM BUDGET CUTTING IN 2018

One of the major findings of the Forum's most recent comprehensive dive into City finances – *Making Ends Meet*, published in September 2016[5] -- was that whatever limited revenue growth the City had experienced in the 2011-2015 timeframe, it had allocated to the public safety function. That reflected the priority of policymakers to protect MPD (and to a lesser extent, MFD) from personnel cuts, leaving other departments to bear the brunt of any budget cutting required in those years.

Perhaps the most significant element of the 2018 proposed budget is that it ends that prioritization. With the $22 million increase in the City's employer pension contribution and other cost-to-continue pressures necessitating substantial departmental cuts, public safety essentially is treated like all other functions. And, because MPD and MFD account for 65% of all general fund expenditures, the cuts look particularly severe.

As noted above, the proposed budget would reduce MPD expenditures by $8.7 million and MFD expenditures by $10 million. Sworn strength at MPD would be reduced by 33 police officer positions, and 75 positions would be eliminated from MFD (no layoffs would be involved in either department, as the reductions in both departments would occur through attrition). MFD is hit particularly hard in the proposed budget; it would see three fire apparatuses decommissioned and two indefinitely shut down (also known as "browned out"). Perhaps more significant, six fire houses would be closed for fire and rescue purposes (though three of the six would be used for other purposes).[6]

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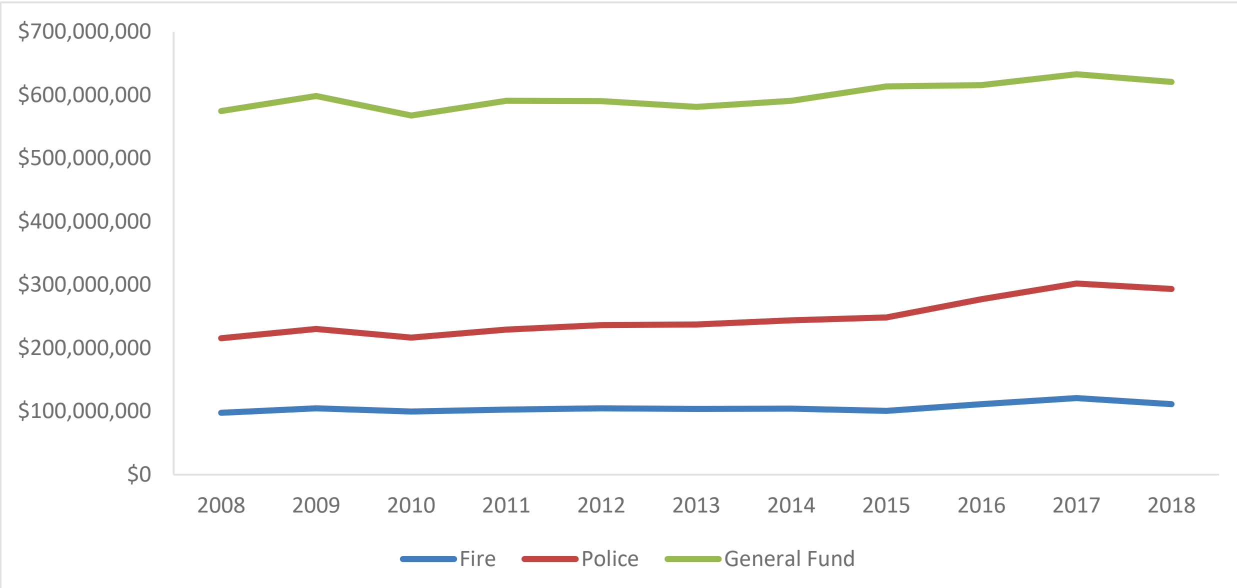
[5] Report can be accessed at https://publicpolicyforum.org/research/city-milwaukee%E2%80%99s-fiscal-condition-making-ends-meet.

[6] Despite these changes, City officials have indicated that MFD response times will not significantly increase.

Chart 6 shows that despite the proposed cuts in 2018, both MPD and MFD would have substantially higher expenditure budgets than they enjoyed a decade ago. If the proposed budgets are adopted, then MPD's budgeted expenditures will have grown by $77.9 million (36%) when compared to 2008, while MFD's will have grown by $13.6 million (14%). By comparison, overall budgeted general city purpose expenditures will have grown by only $46.1 million (8%) over that period, which illustrates how public safety budgets grew at the expense of other general fund departments.[7]

Chart 6: Police, fire, and general fund budgeted expenditures, 2008-2018 (in millions)



It also is important to note that despite the proposed cuts to public safety budgets in 2018, other departments are not spared. As shown earlier, several other departments would see expenditure reductions, including the Department of Public Works, Department of Administration, Milwaukee Public Library, and Department of Neighborhood Services.

Nevertheless, the cuts to public safety stand out in the proposed budget, and that is no accident. The decision not to spare police and fire is firmly linked to a call by the Mayor for a proposed half-cent city sales tax, the proceeds from which would be allocated exclusively to public safety. The budget estimates the proposed tax would generate $35 million annually, which amounts to about 9% of the combined public safety budgets proposed for 2018. The Mayor is seeking authorization from the State to put the proposed sales tax before voters in a binding referendum on the April 2018 ballot. If adopted, it would enable the City to increase police sworn strength to 1,900 officers from the current 1,855, and recommission the two browned out fire apparatuses.

The budget also notes that the need for a public safety-dedicated sales tax is at least partly attributed to the City's inability to control salary and benefit costs for sworn police and fire employees to the extent it has been able to do so for non-public safety workers. Wisconsin Act 10

[7] Expenditures for MPD and MFD increased sharply in 2017 because their budgets reflect retroactive salary increases agreed upon as part of contract negotiations with police and fire unions that culminated in 2016.

does not apply to protective service employees. Hence, while the City has been able to agree with its public safety unions on some changes to pension benefits that resemble those made for other employees, the need to collectively bargain both pension and salary adjustments will limit its ability to control wage increases and make additional pension adjustments going forward.

In *Making Ends Meet*, we predicted that "if maintaining MPD staffing levels continues to be a top priority – and if health care costs begin to rise and revenue streams continue to exhibit little growth – then it is likely that non-police services will begin to suffer." The Mayor's 2018 proposed budget indicates that he is unwilling to continue to protect MPD (and MFD) while other functions of City government experience all the pain from the City's structural imbalance.

His message is clear: without some form of revenue injection, public safety and other functions will have to bear an equal share of the City's annual budget cutting burden. Whether the Common Council agrees with that paradigm shift will be the key point of deliberation in the weeks ahead.

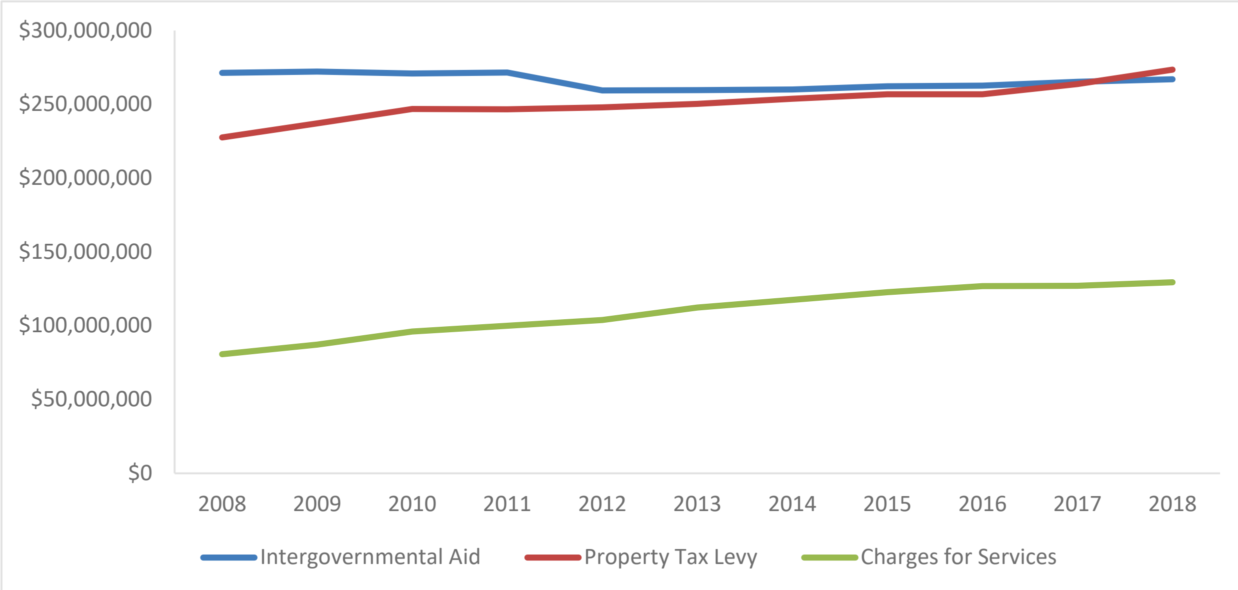
PROPERTY TAX LEVY GROWS BY 3.7%; GROWTH IN 4% RANGE COULD BECOME THE NORM

In *On the Money?*, our July 2017 report that conducted an in-depth look at the City's revenue structure, we found that Milwaukee is unique among its national peers in its reliance on intergovernmental revenue (mainly from the State of Wisconsin);[8] and in its State-imposed restrictions on local taxing authority that leave the property tax as its sole means of local taxation. In fact, our analysis found that in 2012 – the most recent year for which comparative data were available – Milwaukee was third among 39 peer cities in its receipt of State aids as a percentage of its governmental revenue (48%) and first in use of property taxes as a percentage of local taxes (96%).

A major development in the 2018 proposed budget is that – for the first time – the property tax jumps ahead of intergovernmental revenue as the largest single revenue source in the City budget. This results from the fact that intergovernmental revenues have been stagnant for years, which has placed considerable pressure on City leaders to raise both property taxes and service charges. Chart 7 tracks the three revenue sources over the past decade and shows that intergovernmental revenues decreased by 2%, while property tax levies grew by 20% and charges for services by 61%.

[8] Aid from the State's Shared Revenue program comprises the vast majority (82%) of the City's intergovernmental revenue.

Chart 7: Trends in City's three largest revenue sources, 2008-2018 (in millions)



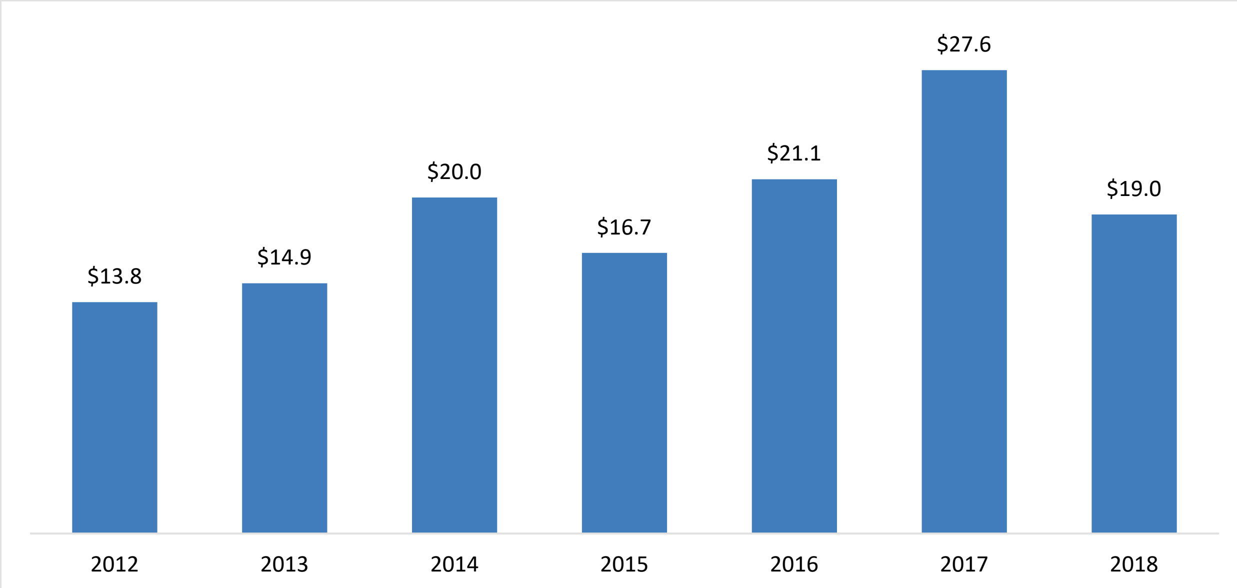
Barring inflationary growth in shared revenue and other intergovernmental revenue – or State authorization to pursue a City sales tax – these trends are likely to continue and perhaps accelerate. In 2017, the City's property tax levy grew by 2.8% and service charges grew by less than a percentage point. In the 2018 proposed budget, the property tax levy grows by 3.7% ($9.7 million) while total service charges grow by 2% (though as shown in **Table 1** above, major resident-based service fees grow by 3%).

The proposed budget warns that barring new revenue sources or increased State aids, "maintaining the *reduced* 2018 proposed budget expenditures through 2022 will require an annual tax levy increase between 4% and 5%." Whether annual increases of that magnitude even will be possible is questionable, as the State currently caps property tax growth at the annual percentage increase in new construction.[9]

Another factor that could impact the growth of property taxes in future years is the City's ability to sustain large annual draws from its Tax Stabilization Fund (TSF). The TSF exists to help the City avoid wide swings in the property tax levy from year to year in light of the potential negative impacts on service levels. For 2018, a TSF withdrawal of $19 million is proposed, which is a decrease of $8.6 million from 2017. **Chart 8** shows that the 2018 proposed amount is more in line with draws made from 2014-2016, though still above withdrawals from the two years before that.

[9] Property tax limits also involve specifications involving carryovers of "cap space" from previous years and other factors that may allow for growth that exceeds the rate of new construction in certain years.

Chart 8: TSF withdrawals, 2012-2018 (in millions)



The City's ability to make large annual withdrawals from the TSF is predicated on its ability to replenish the fund on an annual basis with operating budget surpluses. Significantly increased draws have been made possible in recent years by huge health care savings, which have helped to create large surpluses to deposit into the TSF. Such health care savings are expected to be largely exhausted after this year, however, which means that fund replenishment will revert to levels experienced before the City first began to enjoy significant health care savings in 2012.

As of the beginning of 2017, the TSF balance was $50.7 million, which is a healthy amount but $10 million less than the previous year. The lower fund balance necessitates the reduction in the withdrawal from 2017 to 2018. While the City is expecting another large health care surplus in 2017, other budgetary factors are likely to preclude substantial replenishment again this year, which means the TSF withdrawal in 2019 again may need to decrease. Should TSF withdrawals return to the $13-$15 million range experienced in the previous decade, there will be additional pressure on the property tax to make up the difference.

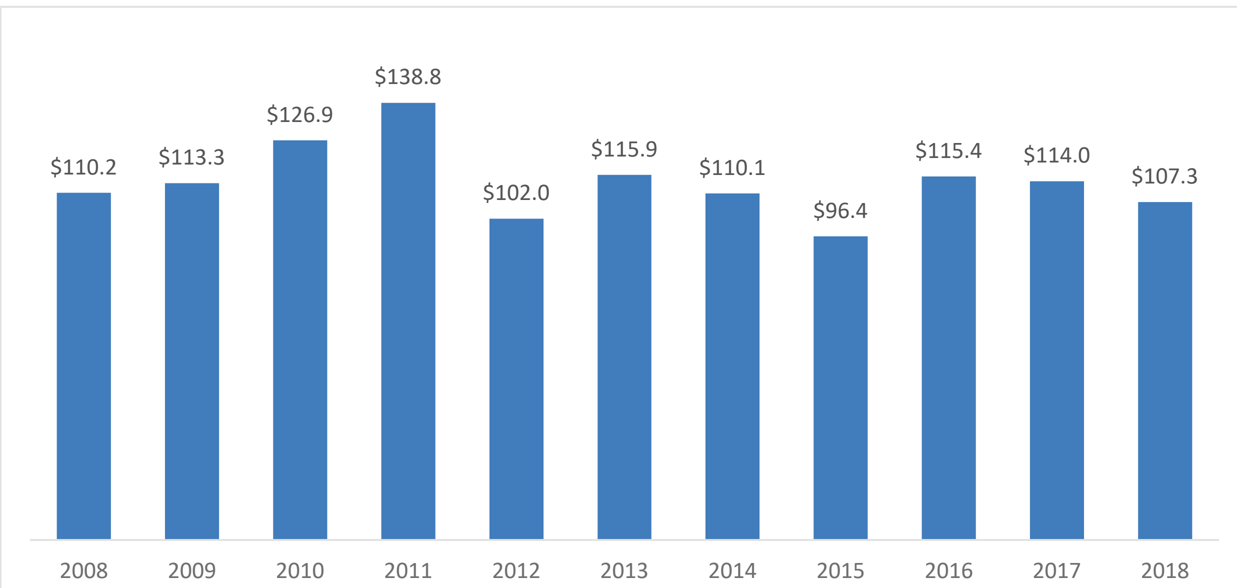
Overall, the lack of growth in intergovernmental revenue, a diminished ability to make $20 million-plus annual withdrawals from the TSF, and the absence of other local revenue options will continue to put severe pressure on the property tax and service charges for the foreseeable future. With nowhere else to turn to offset growing salary and fringe benefit costs – particularly for unionized public safety employees – City leaders likely will have little choice but to continue annual increases in those revenue sources that exceed the rate of inflation if they hope to maintain service levels.

ANOTHER YEAR OF HEALTH CARE SAVINGS HELPS CUSHION BUDGETARY PRESSURES

As we discussed in detail in *Making Ends Meet*, health care savings were the key to budget solvency for the City from 2011 through 2015. As shown in **Chart 9**, prior to 2011 – when City leaders adopted a series of changes to the City's employee/retiree health care structure and benefits – health care costs increased substantially from year to year. However, the 2011 changes – coupled with additional significant changes in 2014 – allowed the City not only to avoid budgeting for annual increases, but also produced substantial budgetary savings in most years that could be used to address other needs. Those savings were particularly critical to the City's ability to accommodate the sharp spike in its annual employer pension contribution discussed above.

After a budgeted increase in 2016 and a small budgeted decline in 2017, health care costs were expected to increase again in 2018 and resume annual growth of 3-5%. In fact, in our 2017 budget brief, we projected such an increase in 2018 "barring another set of changes to the benefit structure or increased employee cost sharing." Yet, instead, the proposed budget projects health care expenditures of $107.3 million – a decrease of $6.7 million (5.9%) from the amount budgeted this year. This is extremely fortuitous given the $22 million increase in the employer pension contribution.

Chart 9: Budgeted health care expenditures, 2008-2018 (in millions)

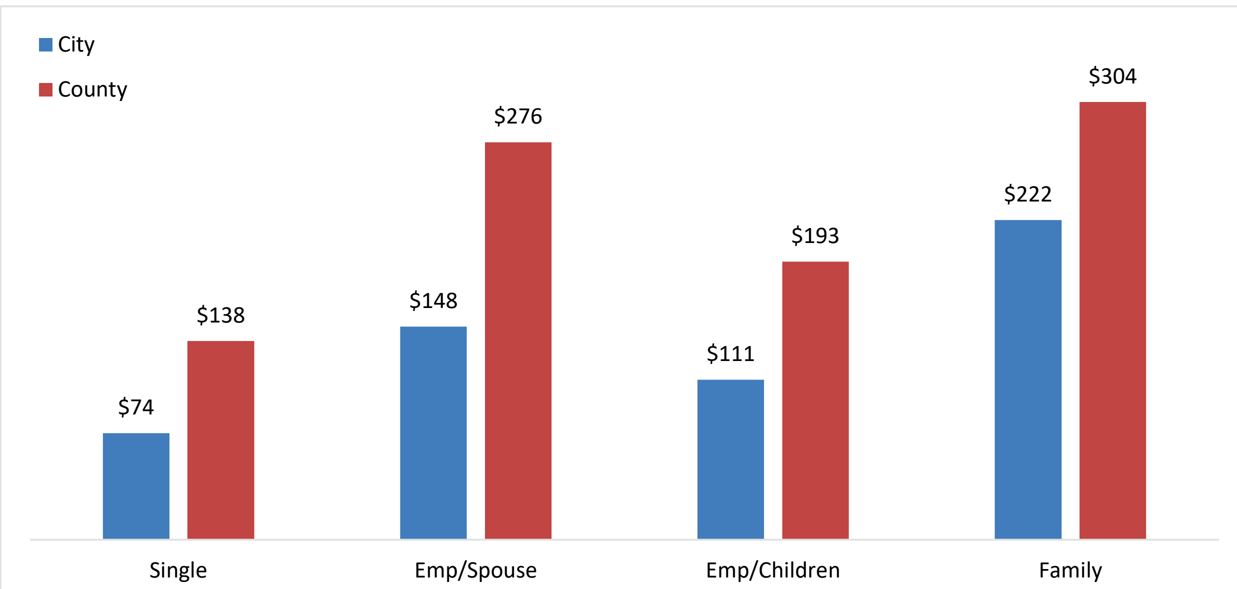


Budget officials attribute the additional year of unexpected savings to substantial projected underspending in 2017 caused by lower-than-expected health care utilization and claims. Consequently, while they still expect inflationary increases in costs for 2018, they are able to apply that increase to a much lower 2017 baseline than the budgeted amount of $114 million. It is estimated that actual health care spending in 2017 will be at least $10 million under budget.

City employees have been another beneficiary of the continued savings from the health care budget, as City leaders have been able to spare them from increased cost sharing. In fact, the employee share of monthly health care premiums has gone unchanged for the past six years. This is in stark contrast to Milwaukee County, where employees have been asked to contribute more in almost every year during that same timeframe. In fact, as shown in **Chart 10**, proposed monthly health care premium contributions for City employees are well below those of their County counterparts (this assumes the contribution levels contained in the County Executive's 2018 recommended budget are adopted).

While it is impossible to determine whether the County is asking too much of its employees – or the City not enough – this finding does suggest the City may have room to consider increased employee health care contributions once its expenditures begin to rise again (which could occur as soon as 2019). Of course, the precise nature of the health care benefits offered to employees also must be considered in determining their appropriate premium contributions.

Chart 10: 2018 monthly health care premium contributions from City and County employees



Source: Milwaukee Department of Employment Relations, Milwaukee County 2018 Recommended Budget

CAPITAL IMPROVEMENTS BUDGET IS TRIMMED AS CITY SEEKS TO CONTROL BORROWING

The Forum's multi-part series of reports on local government infrastructure has looked so far at City-owned streets and bridges, City-owned water and sewer pipes and treatment plants, and City buildings. We have found substantial challenges, as the needs associated with aging infrastructure contradict the City's imperative to control property tax levy-supported borrowing in light of the many pressures on the City's finite property tax levy that have been discussed throughout this report.

Two of the City's most pressing capital needs involve projects to repair the foundation of City Hall and to renovate the Police Administration Building (PAB). In 2017, the City appropriated $13 million of levy-supported general obligation (G.O.) bonding for the City Hall project, and $5.5 million for PAB renovations. As we discussed in our most recent infrastructure report – *Cracks in the Foundation*[10] -- because it has been required to accommodate substantial amounts of borrowing for those projects, the City has borrowed and spent less than might have been desired on basic building repair needs and the needs of other capital assets.

Despite the competing obligations to complete the City Hall and PAB projects while also catching up with other capital needs that have been deferred, the 2018 proposed budget reduces total capital improvements spending by $8.2 million (5.4%) and decreases levy-supported G.O. bonding and cash by $12.7 million (13.5%). Furthermore, while $9 million in G.O. bonding is appropriated for the City Hall project, that amount is less than had been anticipated previously and may result in the project being extended for an additional year. Meanwhile, the PAB project would receive no funding, as work would be continued with appropriations from previous years, again potentially resulting in a delay in completion. Borrowing for other building needs also would decrease by $3.7 million, while borrowing for City streets would decline by $1.1 million.

The effort to reduce levy-supported G.O. borrowing in 2018 stems from a desire to comply with a long-time policy goal of limiting the amount of new borrowing each year to no more than the amount of levy-supported debt that comes off the City's books that year. The goal is designed to ensure that annual levy-supported debt service payments do not grow from year to year, thus preserving tax levy resources for other needs.

In a typical year, the City retires approximately $70 to $75 million of levy-supported G.O. debt. However, as shown in **Chart 11** (on the following page), annual levy-supported G.O. borrowing substantially exceeded that amount from 2014 through 2017. The proposed amount of levy-supported borrowing in 2018 would put the City in range of the policy goal.

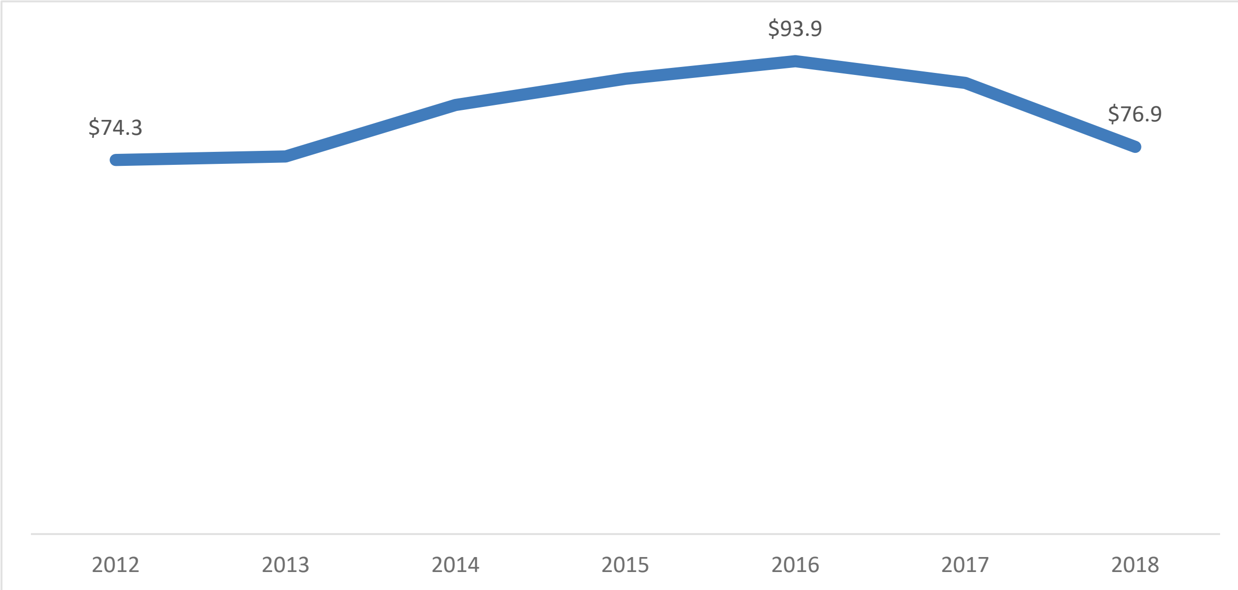
Capital Spending for Milwaukee Water Works and Sewer Maintenance Fund

The Milwaukee Water Works (MWW) and Sewer Maintenance Fund (SMF) do not use tax levy-backed G.O. bonding to support their capital projects, but they do use revenue bonds that are backed by sewer and water fees. MWW would see a $5.4 million increase in revenue bonds in the proposed budget, as $27.3 million of borrowing is recommended. Contributors to the increase include the need to replace 18 miles of water mains as mandated by the Public Service Commission, as well as replacement of lead service lines.

Conversely, the SMF would see borrowing reduced by $1 million from 2017 and by $4 million from the amount requested by the Department of Public Works. According to budget officials, this reflects a determination that the City was exceeding its goal of repairing or replacing all sewers every 90 years, and instead had reached a 75-year interval. The City's goal to repair and replace 27 miles of sewers per year continues, however.

[10] The report can be accessed at https://publicpolicyforum.org/research/cracks-foundation-analysis-building-repair-and-replacement-needs-city-and-county-milwaukee.

Chart 11: Levy-supported G.O. bonding for capital expenditures, 2012-2018 (in millions)



The desire to reduce annual G.O. borrowing certainly is appropriate from a fiscal standpoint. However, to the extent that prudent controls on borrowing conflict with needed infrastructure projects, other problems could emerge. For example, if such controls require the City to defer projects involving basic repairs to buildings or streets, then the cost of those repairs could escalate, or basic repair projects could turn into projects involving full-scale replacement. In addition, as a backlog of needed projects develops and grows, it can become so overwhelming that it simply cannot be resolved. As we have pointed out in our infrastructure series, that is precisely the paradigm facing Milwaukee County as it has similarly attempted to control borrowing in a manner that has conflicted with its infrastructure obligations.

The effort to control borrowing in 2018 is unlikely to cause an infrastructure crisis for the City, but several successive years of strict controls could be problematic. This is a situation that should be monitored closely by both budget and public works officials in the years ahead as the City struggles to find a "sweet spot" between affordable levels of borrowing and responsible management of capital assets.

CONCLUSION

In the Introduction to this report, we describe the 2018 proposed budget as a “watershed” budget for the City. That description is based on the fact that this is a budget of firsts. For the first time since 2010, the Milwaukee Police Department would not be protected from the City’s annual budget cutting endeavors; and for the first time since creation of the shared revenue program, the City’s property tax levy would eclipse intergovernmental revenue as its single largest source of revenue.

These two developments, of course, are inextricably linked to the annual deficits caused by the City’s faulty revenue structure and personnel-related expenditure pressures. The Mayor’s determination that public safety functions cannot be shielded reflects a conclusion that other departments cannot bear the full brunt of the substantial deficit reduction required for 2018. Meanwhile, the growth in property taxes similarly is reflective of the magnitude of next year’s deficit reduction challenge. The proposed budget’s unmistakable message is that with intergovernmental revenues largely flat and nowhere else to turn on the revenue side, *all* City services must be subject to reduction and the property tax levy must continue to grow.

A potential bright spot is that while the City does face a long-range structural imbalance, the deficit reduction challenge for 2018 is particularly acute. That challenge is driven by a $22 million increase in the employer pension contribution, but the contribution should stabilize over the following four years. Consequently, as the budget notes, successfully funding the increased pension contribution through the elimination of positions and expenditure reductions should “improve the near term outlook.”

Yet, the City faces other growing financial challenges, including the likely return of annual inflationary increases in health care expenditures, an escalating list of capital needs that runs counter to its desire to limit borrowing, and the need to accommodate growing public safety personnel costs that cannot be controlled through the Act 10 toolbox. Hence, while the severe fire and police cuts required in 2018 may not need to be fully replicated in the near-term future, continued public safety service and position reductions and 4-5% annual property tax levy growth may need to become the norm.

While the Mayor has determined that MPD no longer should be off limits when it comes to personnel and expenditure reductions – and that budget cutting at MFD should eclipse previous proposals -- the Common Council may disagree. Making up the millions in savings that result from the proposed reduction of 108 public safety positions would not be easy, and likely would necessitate much deeper cuts in public health, libraries, and neighborhood services, or an even bigger property tax increase than that proposed by the Mayor. Nevertheless, that is where legitimate policy deliberation can and should occur. Less legitimate would be consideration of one-time options, such as depletion of reserves.

Overall, the difficulties posed by the 2018 budget are emblematic of a financial structure that needs to be fixed. While the nature of the fix is debatable, the underlying causes are apparent and should no longer be ignored.