

Friends,

If you've tracked City government at all, you've probably heard the Mayor, Councilmembers or Staff talk about "buckets" or "funds". You've probably heard us talk about our ability to pay for some services and our inability to pay for other services as if our hands were somehow tied – as if we somehow do not control how to spend taxpayer money. How can this be?

You have also may have looked at City spending and thought "That just doesn't make any sense". You may have heard about the possibility of firefighter layoffs (averted for the time being) while at the same time seen progress on construction of an underground parking structure on the Downtown Library Lot, or heard about investments in single-stream recycling while driving over the degraded Stadium Bridge. How can it be that the City on the one hand can claim revenue distress, while at the same time, go out and begin construction on these other projects? These are reasonable questions. Let me try to answer them.

### **Multiple Funds**

The bottom line is that the rules that govern municipal revenues, expenditures and accounting are very different from the rules that apply to us all as private citizens.

Like you, my family has one checking account – our income gets deposited into that account; our bills get paid from that account. If we need to pay the gas bill, buy groceries, fix the roof, pay the mortgage, it all comes from that one account – that one bucket. In this case, money is truly fungible. If the roof needs fixing, we have less money available for groceries; if our gas bill is low because we've turned down the thermostat, we have more money available for groceries.

The City does not work this way; it cannot work that way.

The City is a highly complex organization with anticipated revenues in excess of \$350M this year. To organize these revenues and their associated expenditures, therefore, the City maintains a variety of separate accounts – called Funds. The City maintains these Funds as separate accounts for a variety of reasons; in some cases it is legally required to only spend certain monies for certain purposes, on other cases, the City has decided to segregate a service function to better understand its operation.

Those are the general principles – let's get to specifics, let me sketch some of these Funds these for you:

**General Fund** – The General Fund (approx. \$82M in FY 2010) is the chief operating fund of a local government. This fund is primarily funded by taxes (as opposed to user fees) and expends money for activities that are not financially sustainable without support for taxes. For example:

- Police
- Fire
- Most park operations (e.g., mowing the grass)
- Recreation
- 15<sup>th</sup> District Court

Within the General Fund, monies are indeed fungible – monies not spent on Parks can be spent on Police salaries. In FY 2010, approximately 48% of the General Fund budget goes to Safety Services (Fire & Police).

**Special Revenue Funds** – The City may establish a Special Revenue Fund to account for the proceeds of specific revenue sources. State or Federal law typically restricts the City’s ability to spend monies from these sources to a set of limited areas. Examples include:

- Parks Improvements Millage – Restricted by the specific millage language approved by voters.
- Major Streets - Revenues come primarily from State gasoline and weight taxes. The State restricts expenditures to repairs, maintenance and construction on the City’s major streets.
- Federal and State Grants – Monies are legally restricted for the purpose of the specific grant.

These voter-approved taxes or government grants cannot be used for any purpose other than the one designated up front. So, for example, we may appear well funded with some “Parks” money by virtue of the Parks Improvement Millage, but because these are “improvements” monies, we cannot use them for “operations” – to mow the grass or groom the baseball fields. Operations monies must come out of the General Fund, where budget pressures are severe.

**Enterprise Funds** – Enterprise Funds are internal accounting conventions used to account for operations (a) that are financed and operated in a manner similar to private business enterprises – where the City intends that the costs of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where it is useful to track revenues earned, expenses incurred, and/or net income for capital maintenance or other purposes. The City utilizes enterprise funds for activities such as:

- Water
- Sanitary Sewer
- Ann Arbor Airport
- Farmer’s Market
- Solid Waste
- Golf Courses

The primary benefit of an Enterprise Fund is to give the City the data to determine the profit or loss associated with a particular service. Consider the City's Golf Courses. These amenities run at a loss of hundreds of thousands of dollars a year. Over the past few years, the City has determined to turn these facilities around. With the data provided by Enterprise Fund accounting, we can accurately determine the revenue and true costs associated with running these business-like ventures. Although there is still much work to do, the City's efforts are bearing fruit; Golf is still a drain on the budget, but there has been a substantial improvement.

Enterprise Funds also enable us to better plan to meet needed capital improvements in capital-intensive departments. Water rates, for example, cover the day-to-day cost of water delivered, but because we have created a separate Enterprise Fund, we are also able to determine what rates are necessary to cover long term infrastructure needs, like new treatment plants or water main replacements.

**Internal Service Funds** – These Funds are used to account for goods and services provided by one City department to other City departments. For example:

- Information Technology
- Fleet Services

These Internal Service Funds provide valuable cost-cutting information. Take this example – software licenses. Software licenses cost the City hundreds of thousands of dollars each year. If that cost were paid for by a General Fund IT line item, there would be little direct incentive for managers throughout the City to be efficient in their use of software. If, however, each manager's budget is charged for each software license used in that area, then managers are going to carefully determine what they need and eliminate wasteful licenses.

### **OK, so what?**

Understanding the 'buckets' enables you to understand that in the City there is often money usable for one purpose, but not usable for another purpose. Understanding the limitations imposed by various Funds helps you understand why the City does what it does.

Take the Library Lot, for example. It seems peculiar that construction on an underground parking structure should begin at the same time as we were nearly required to lay off firefighters (Note that the reprieve is really only for 6 months; the conversation will begin anew this spring). Aren't the firefighters more important than a new structure? Arguably yes, but the money for the Library Lot parking structure could not be used to pay firefighter salaries – the money to pay to construct the structure will come from the parking lot itself through a fund controlled by the Downtown Development Authority ("DDA"). In other words, a

decision to forego the Library Lot parking structure would not increase the General Fund – it would not increase the money available to pay for Safety Services or to pay to mow park grass.

Consider too Council's recent decision to invest \$4.5M+ in single-stream recycling. The benefits of this program will be as follows: 1) We would now be able to recycle more materials – all plastic bottles, household plastic containers #1,#2, and #4-7 (no styrofoam or #3s), and bulky HDPE such as buckets, crates, toys, trays, and furniture; 2) A RecycleBank rewards system that should net the average household approximately \$240 in consumer-specified coupons redeemable at local businesses; 3) An increase in waste stream diversion from 50% now to 70%; and 4) A cost savings to the City of between \$500K - \$750K per year.

These are obviously substantial benefits to our community, but you might reasonably observe that these benefits might not be as important to Ann Arbor as, say Stadium Bridge. The money that will be used to fund the single-stream investments, however, cannot be spent on bridge infrastructure – it comes from reserves in the Solid Waste Fund, a fund supported by the Solid Waste Millage and sewage fees. It would be, therefore, illegal to use that money for anything unrelated to waste stream management.

**Bottom line.**

Running a City is a complex operation subject to legal, contractual and 'best practices' limitations on the freedom of the City to spend tax, user fee and other revenue.

These limitations often result in unbalanced resources – one area of the City's Budget may be deeply underfunded (e.g., the General Fund), whereas another might be secure (e.g., the Water Fund). These limitations prevent the City from freely shifting its resources from flush Funds to impoverished Funds, even though we might all believe it to be a "better" use of those resources. In the end, these restrictions are a fact of life and we will do our best to provide the services that Ann Arbor demands with the resources entrusted to us.

Please of course do not hesitate to contact me with regard to any questions you may have about this, or any other City matter. If these budgetary conversations interest you, please see <http://www.a2gov.org/OurTown> for details.

Best,

Christopher

P.S. As ever, if you do not wish to receive communications such as this, please just let me know and accept my apologies for the intrusion.