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March 22, 2016

The Honorable Mayor Alan P. Krasnoff and Members of City Council
City of Chesapeake, Virginia

Dear Mayor Krasnoff and Members of City Council:

Today, I am pleased to submit the Proposed Operating Budget for Fiscal Year 2017. Prospects for the immediate future are far more positive than in the recent past, as we are finally seeing meaningful growth in tax collections along with a moderation in the cost of employee benefits. General fund revenue is projected to be 3.3% above the FY 2016 budget with real property values (reassessment plus new construction) increasing by 3.2%. While the local economy continues to underperform the nation, as a whole, due to the impacts of federal sequestration, the city's revenue trends are showing definite improvement. We are much more confident about the future than was the case in past years. We also believe current growth rates will be sustained over the next three to five years.

For FY 2017, we propose a spending plan that totals $967.5 million for the Operating Budget. This represents an increase of $29.6 million or 3.2% of the FY 2016 budget. Increased costs are largely attributable to public schools, service gaps in several City departments, and additional debt service requirements. The budget does not include any significant service expansions; however, a number of staff adjustments are necessary in order to improve service delivery.

Council's Guiding Principles

The FY 2017 Operating Budget was developed with guidance from City Council including the following principles that have served as a foundation of Chesapeake budgets for the last several years:

- No increase in the real estate tax rate,
- No new fees (though increases in existing fees may be considered),
- No supplanting of losses in state or federal funds with local revenue,
- Review all vacant positions for possible elimination,
- Identify operating efficiencies and reduce spending accordingly, and
- Identify non-core services for possible consolidation, curtailment or elimination.

This budget proposal is consistent with the Council's guiding principles. The proposed budget assumes that the real estate tax rate will remain constant, currently $1.05 per $100 of assessed value (including the Mosquito Control tax). While no *new* fees are required for this budget proposal, the budget includes an increase in water and sewer utility rates of 4.9%. The scheduled rate increase will take place July 2016 and is the fourth of five planned increases. The rate increases are necessary to maintain a stable enterprise fund and to allow for system improvements required by emerging environmental regulations.

No other changes are proposed in tax rates or fees for services.

Budget Drivers

For much of the last decade, the City's General Fund revenues have either fallen or grown by very small amounts. However, in FY 2015, General Fund revenues grew by 3.2%. Perhaps more importantly, nearly the entire 3.2% represented real growth, since the rate of inflation was near zero for the same period. We believe the results would have been even better had federal austerity efforts not taken place. For the next several years, we project that General Fund revenue will grow by approximately 2.2% annually.

Fortunately, we are in a period of relatively low inflation and most cost increases have been moderate (during calendar year 2015, the Consumer Price Index rose just 1.37%). Energy costs have dropped steeply during the last two years and are expected to rise only moderately in the coming years. While the energy sector is very volatile, it appears prices will remain well below historic highs throughout FY 2017. Health care costs remain an exception to the overall low inflation. A combination of employee utilization of health care related to an aging population, new medical technologies, and rapidly growing pharmacy costs requires greater contributions from both the City and employees.

For FY 2017, we will experience significant reductions in retirement costs. The employee retirement program is recovering from losses sustained during the recession and the latest actuarial report reduces employer contributions from 15.93% of employee pay to 13.71%. The reduction in employer pension contributions saves $2.5 million for the General Fund. Additionally, the availability of affordable options on the public health exchange for Medicare-eligible retirees has reduced the City's annual contributions to the OPEB Trust Fund by over $5 million.

Other major changes in government costs proposed in this budget:

- **Productivity Enhancements**: The Budget Review Committee reviewed requests for 50 new positions (FTE) from departments throughout the City. After a thorough inquiry and analysis of departmental requests, we recommend the funding of 44 full-time equivalent positions (FTE). Practically all of the new positions are funded with new programmatic revenue, by reducing other expenditures, or from enterprise revenue. The newly funded positions:

  - ✓ Ensure effective use of scarce resources by lowering overtime and temporary service costs,
  - ✓ Address new service demands that are funded with new revenue, and/or
  - ✓ Improve the City's response to citizen service demands.

  Most of the new positions are needed for the water and sewer utility fund (9.0 FTE) and for Chesapeake Integrated Behavioral Healthcare (17.45 FTE). The utility fund is supported exclusively with user fees and the added positions in CIBH are related to a statewide effort to improve the delivery of behavioral health services. FY 2017 also represents the first year of a three year planned program to increase the authorized number of City Police Officers by at least three officers per year. A listing of the new positions costing $2.7 million appears in Section B of the budget document.

Additionally, we are recommending spending that will allow the installation of GPS tracking devices on some vehicles in the City fleet. The devices will allow supervisors to locate vehicles in emergency situations, review and monitor driving patterns, assist in routing and scheduling, and identify unauthorized usage. The budget includes funding to begin the program for Public Works and Parks, Recreation & Tourism. We are also considering additional departments for future funding.

- **Employee Compensation:** The FY 2017 operating budget includes a 2.5% general wage increase effective July 1, 2016 for employees hired prior to January 1, 2016. It also includes a provision for performance recognition and a wage compression adjustment for eligible part-time employees (eligible full-time employees have already received compression adjustments). Both the performance recognitions and the compression adjustments would be effective October 1, 2016. The total cost of employee pay enhancements planned for FY 2017 is $5.8 million.

  We also recommend that future general wage increases apply to all eligible employees, regardless of status (full-time, part-time, seasonal, special projects, etc.).

  <u>Career Paths for Public Safety Employees:</u> the FY 2016 budget included funding to implement career paths for rank and file police officers, fire fighters, and Sheriff's deputies starting January 2016 (actual implementation has been delayed to spring 2016). The initiative establishes a compensation and recognition system designed to reward employees for their contribution to the organization, as demonstrated by the successful application of the desired knowledge, skills, abilities and competencies. The FY 2017 budget includes a full year of funding for the career path initiative.

  Competitive Wage Rate: Currently, the City's competitive wage rate (i.e. living wage) for regular full-time employees is established at $10.15 per hour. Based on a review of the change in the Consumer Price Index and U.S. Federal Poverty Guidelines, we recommend an increase to $10.30 per hour (1.5%).

- **Healthcare**: Even as the City has taken steps to reduce the growth in employee health care costs, medical claims for the most recent contract period were significantly above estimates. While retiree utilization of health care outpaces that of active employees, increased claims by all participants resulted in a double-digit increase in the renewal terms for the plan year beginning January 2016. In order to hold premium increases to 8%, the City selected a three-pronged approach. First, it moved from a fully-insured plan to a self-insured plan starting January 2016. While the City assumes greater risk under the new funding model, we believe the self-insurance plan will provide new opportunities that benefit all participants and help to stabilize costs in the long run. The second strategy was to strengthen the employee wellness program by providing greater incentives for employees to get full physicals from their physicians. Finally, it was also necessary to adjust benefit and cost sharing levels.

- **Long-Term Disability**: As required, employees in the VRS Hybrid Plan are provided employer-paid short and long term disability benefits. While permanent disability benefits are available to employees in VRS Plans 1 and 2, temporary disability benefits are not available. In an effort to provide 40% income replacement to VRS Plan 1 and 2 employees who become temporarily disabled, the budget includes employer-paid <u>long-term</u> disability insurance for Plan 1 and 2 employees. We have budgeted $150,000 to meet the estimated cost of this benefit. Eligible employees will have the opportunity to purchase additional coverage up to 60% of their annual wages.

- **Conversion of Mainframe Positions**: As the City transfers mainframe applications to server platforms, a number of positions are being eliminated and replaced with positions required in a client-server environment. The total number of positions does not change and the overall wage and benefit costs are substantially unchanged. We expect that the roles of twelve (12) employees/ positions will be substantially different once the transition is complete (21% of IT staff). Affected positions include software systems programmers, systems analysts, and computer operators. The department will work with Human Resources to transition affected employees.

- **Payroll Efficiencies:** Employees are paid in two payroll cycles: weekly and semi-monthly. Weekly employees are paid in arrears, generally five to seven days after the last day of their pay cycle. Semi-monthly employees are paid current rather than in arrears (on the 15th and 30th day of the month) causing significant rework and added procedures in order to avoid overpaying employees who are absent from work. The FY 2016 budget included a $3.5 million provision for implementation of pay cycle changes that we now recommend postponing until FY 2017. The delay is primarily caused by conflicts with plans to provide employee pay raises in July. We recommend continued funding for the pay cycle changes in the FY 2017 budget from a one-time draw on the General Fund balance that will remain on June 30, 2016. The provision has been adjusted by current and recommended changes in employee compensation.

  The implementation provision will be used to provide bridge pay to employees as they transition from current pay to arrears pay. Without the transition adjustment, employees would realize a one-week lapse in pay. We estimate that the transition payment will range between five and seven days depending on the employee's work schedule. We also propose to forgive 20% of the transition advance in each of the following five years. Employees who remain with the City five or more years would not repay the transitional advance. For employees leaving employment before the end of the five years, all or a portion of the advance would be recaptured from the final wage and leave payment.

- **Debt Service:** In FY 2016 the City's payments on its debt dropped by $14 million as it paid off several large debt issues from the mid-1990s. During FY 2017, an additional savings of $5.6 million will occur as payments on existing (pre-lockbox) debt continue to decline. However, the City and School Board expect to issue nearly $90 million in new General Obligation bonds during the Spring of 2016 that will require annual debt payments of approximately $8.5 million annually starting in FY 2017. We have adjusted the FY 2017 budget to recognize the savings in pre-lockbox debt service along with the estimated debt payments related to the Spring, 2016 borrowings. Finally, as we have done in the recent past, we recommend that $5.6 million related to savings from the reduction in pre-lockbox debt be redirected into the City and School capital lockboxes during FY 2017.

- **Chesapeake Jubilee** – in past years, the City budget included a direct cash subsidy to the Jubilee, an annual festival held at City Park. This budget does not include direct cash support for the Jubilee. However, the City will continue to provide approximately $220,000 of direct and in-kind services to the Jubilee from several departments throughout City government.

Looking Forward

In developing the annual operating budget we carefully considered the long-term impacts of current budget decisions. Each department provided a three-year budget that addressed not only their immediate requirements, but also strategic plans and requirements beyond FY 2017. In future years we will also review proposals that have merit and that are consistent with Council's long-range plans. Proposals that meet these criteria and which are sustainable will be recommended for funding.

We requested that department leaders include a three-year spending plan with their annual budget submissions. This permits us to improve long-term planning by linking current budget decisions to future resource requirements. Department spending plans were combined with revenue projections from the five-year forecast completed in October to form the three year projection. A summary of the projection appears on page B-15 of the budget document with underlying assumptions immediately following. We anticipate growth in City revenue from $687 million in FY 2016 to $749 million in FY 2019. City spending, including transfers to the School Board, are expected to rise from $668 million in FY 2016 to $706 million in FY 2019. Based on the best information available, we are confident that future revenue growth will be adequate to address current and foreseeable service demands.

Discussion of Major Funds

General Fund

General fund revenue is expected to grow by $17.3 million to $543 million, or 3.3% above the FY 2016 budget level. Over one-half of the increase ($9.4 million) is related to increases in property taxes as real estate values improve, new construction is brought onto the tax rolls, and the values of personal property (vehicles) grows. Real estate assessments have climbed by nearly 1.5% as the housing market slowly recovers. Stronger growth in personal property taxes are anticipated as residents replace older automobiles and the used vehicle market improves. In total, property tax revenues are expected to exceed pre-recession levels for the first time.

Most of the remaining revenue increase ($7.1 million) reflects growth in collections of business and consumer taxes. Sales taxes, business and professional licenses, recordation taxes and restaurant taxes are especially strong.

Transfers to Chesapeake Public Schools – Under revenue sharing procedures in place since 2004, most local tax revenues are shared with and allocated to Chesapeake schools on a formulaic basis. Initial allocations are based on projected revenues, but are trued-up after the end of each year. For FY 2017, the revenue sharing formula provides $187.6 million dollars for the School Operating Budget, an increase of $7.4 million (4.1%) above the FY 2016 allocation. We also recommend continued sharing of surplus funds in the Greenbrier TIF; school transfers include $1 million of the Greenbrier TIF surplus.

Actual transfers to schools differ from the annual allocation because of the revenue sharing true-up and reversion of unspent appropriations from previous years. The budget for both FYs 2016 and 2017 include money that was carried over from the previous year. Below is a comparison of all operating transfers to schools for fiscal years 2016 and 2017.

School Allocations (in millions)	FY 2016	FY 2017	Change	%
School allocation based on revenue sharing formula	$ 180.2	$ 187.6	$ 7.4	4.1%
Recommend declaration of surplus in Greenbrier TIF	1.0	1.0	0.0	-
Reversion of prior year appropriations (for textbooks)	0.0	1.7	1.7	-
Diversion from School Lockbox	1.4	0.0	(1.4)	-
True up based on actual revenue from previous years	0.6	0.0	(0.6)	-
Total transfers to school operations	$ 183.2	$ 190.3	$ 7.1	3.9%

The City also owes the School Board $2.4 million from the FY 2015 revenue sharing true-up; the superintendent has recommended the transfer of the revenue sharing surplus to the school's capital program.

Employee Compensation – General Fund wage and benefit costs actually decline by $923,000 even as employee pay raises are recommended and 15.6 FTE positions are added to the budget. As discussed earlier, the major contributor to lower wage and benefit costs are reductions in retirement and other post-employment (OPEB) costs. Listed below are the major factors that impacted personnel costs in the General Fund budget:

Employee pay raises – 2.5% increase starting July 2016	$ 3.7 million
Employee pay raises – performance awards	0.5 million
Employee health care	0.5 million
New positions (15.6 FTE) and employee reclassifications	1.3 million
Career Path for public safety employees	0.4 million
Worker compensation costs	0.5 million
Savings from employee turnover	(1.0 million)
Revision in employee retirement costs	(1.8 million)
OPEB – revision primarily related to Medicare-eligible retirees	(5.0 million)
Net reduction in personal service costs	($ 0.9 million)

Transfers to Other Funds – General Fund resources support a number of other funds, including several Human Service funds, Chesapeake Integrated Behavioral Healthcare, and the Debt Service Fund. Operating transfers to special revenue and capital projects funds are proposed to increase by $9.5 million primarily because of increases in debt service and capital cash requirements. Transfers are reduced for the Public Assistance, Interagency, Integrated Behavioral Healthcare and Juvenile Services Funds because of savings in retirement costs (VRS and OPEB) and in order to recapture excess transfers during FY 2015. A summary of fund transfers appears below.

General Fund Transfers	FY 2016	FY 2017	Change from FY 2016	
Virginia Public Assistance Fund	$ 7,294,708	$ 5,733,153	$ (1,561,555)	-21.4%
Interagency Consortium	1,450,979	1,414,679	(36,300)	-2.5%
Integrated Behavioral Healthcare	7,805,913	7,610,813	(195,100)	-2.5%
Juvenile Services Fund	2,412,027	1,467,727	(944,300)	-39.1%
Grant Fund (local match)	5,000	5,000	-	0.0%
Debt Services Fund	30,466,966	34,664,280	4,197,314	13.8%
Capital Improvement Funds	13,414,056	21,478,531	8,064,475	60.1%
Total Transfers	$ 62,849,649	$ 72,374,183	$ 9,524,534	15.2%

With respect to the Debt Service and Capital Funds, most transfers are provided from locked revenue discussed below (Fund Reserves and Dedicated Revenue). In preparing the Capital Improvement

Program (CIP), we previously recommended that savings realized from the significant reduction in debt service requirements be reinvested into the Capital Program through the existing capital lockboxes. The proposed FY 2017 budget is consistent with recommendations for the CIP.

Purchased Services – The General Fund Budget for purchased services increases $1.4 million and is primarily attributable to changes in the Police and Sheriff's Departments. In the Police Department, the cost to maintain the new Computer-Assisted Dispatch (CAD) System is $251,000 greater than the system it replaced. The Sheriff's budget requires an additional $1.6 million to pay for the City's commitment to the Hampton Roads Regional Jail Authority. Under the existing agreement, the Authority will house an average of 62.5 more inmates per day starting July 2016. We expect to realize $333,000 of savings in the jail medical and pharmacy contract as more inmates are held in the regional jail. Finally, the City's budget for other purchased services is expected to decline by $118,000.

Allocation of General Fund (GF) Overhead Costs – The City allocates a portion of general and administrative costs to Public Utility, Stormwater, and Chesapeake Transportation System enterprise funds. Overhead allocations are limited to estimates contained in the annual Cost Allocation Report which indicates the portion of GF costs that are attributable to each enterprise fund. Overhead allocations are also limited to available funding in the enterprise or special revenue fund and, in previous years, have varied from 59% of allowable costs for Public Utilities to 91% of allowable costs for the Transportation System. No overhead allocations were made to the Mosquito Control Commission (MCC) as the Commission lacked sufficient resources. Similarly, overhead allocations are not made to other special revenue funds that already rely on the General Fund to meet direct operational costs.

We propose to increase the allocation of overhead costs for each fund in order that general tax funds do not indirectly support the enterprise funds. The FY 2014 Cost Allocation Report indicates the City provides $2.5 million of indirect support to the three enterprise funds and MCC. For FY 2017, we propose recovering $1.725 million as follows:

General Fund Overhead Allocated to Other Funds	FY 2016 Overhead Allocated	Cost Allocation Report (2014)	FY 2017 Overhead Allocated	Portion Recovered
Stormwater Fund	$ 420,000	$ 643,205	$ 550,000	85.5%
Chesapeake Transportation System (toll roads)	100,000	125,056	125,000	100.0%
Public Utility Fund	750,000	1,612,081	1,000,000	62.0%
Mosquito Control Commission	-	126,486	50,000	39.5%
Total Overhead Recapture	$ 1,270,000	$ 2,506,828	$ 1,725,000	68.8%

While we have proposed a significant increase in overhead charges, the increase is more than offset by reductions in OPEB costs realized by each of the separate funds.

Fund Reserves and Dedicated Revenue – The City Charter requires the maintenance of a cash flow reserve equal to six percent (6%) of General Fund revenue. In addition to reserves required by Charter, City Council recently adopted a policy requiring an undesignated fund balance of at least ten percent (10%) in order to address emergencies and other unpredictable events. In order to ensure compliance with the policy provision, Council also requires that we budget for a 12% undesignated fund balance. Since General Fund revenue is projected to rise $18.7 million above the FY 2016 budget, the Charter and

Council policy require that $3.37 million of FY 2017 revenue be retained for cash flow and emergencies. More information is available on the Charter reserves and undesignated fund balances on page B-21.

For FY 2017, operating revenues of $45.5 million are committed to current and future capital purposes through two lockbox mechanisms. Of this amount, $19.7 million will be transferred to the Debt Service Fund and $14.3 million will be transferred to the Capital Projects Funds. The remainder of the locked revenue is committed to future capital projects. Finally, several tax or fee levies are dedicated by City Council or the Virginia State Code for specific purposes. In order to comply with such mandates, reserved funds are either added to the ending fund balance of the General Fund or included in a department budget specifically to address the reservation requirement.

School Operating Fund

In accordance with the Virginia Constitution, school funding is a shared responsibility of the Commonwealth and its localities. Unlike many school divisions throughout the United States, Virginia school districts do not have taxing authority, and are, therefore, fiscally dependent upon the locality in which they are located. For this reason, the school operating budget is part of the City budget. Earlier this month the School Board proposed a $466.3 million operating budget for Chesapeake Public Schools (CPS) that includes:

School General Fund	$ 420,242,671
School Nutrition Services (breakfast and lunch programs)	13,480,517
Federal and State Categorical Grants	27,546,542
School Textbook Fund	2,437,884
Other school funds	2,600,000
Total school budget approved by School Board	$ 466,307,614

Funding for the proposed school budget includes $235.6 million in state funding, $30.9 million of federal grants and other assistance, $4.9 million from school fund balances, and $188.6 million from the City's General Fund. The remainder of the school budget ($6.3 million) is provided by fees, cafeteria sales, and other miscellaneous local revenue. The school spending plan for FY 2017 is $12.8 million (2.8%) above FY 2016 budget and includes a 2.5% pay raise for all school employees.

For many years, Chesapeake has shared growth in general tax revenue equally with the School Board. Further, the City traditionally has reappropriated school funds that were collected, but not spent during the school year. The recommended school budget based on the revenue sharing formula and the reversion of FY 2015 school funds is as follows:

School budget proposed by School Board	$ 466,307,614
Adjust city transfers to CPS based on final revenue projections	(12,000)
Add reversion of FY 2015 school funds for Textbook Fund	1,691,834
School budget included in City budget	$ 467,987,448

As is discussed in more detail under TIF Funds, we recommend that City Council declare a surplus in the Greenbrier TIF at the end of FY 2016 and that $1 million (one-half) of the surplus transfer to the School Board for FY 2017 operations. The $1 million surplus from the TIF is part of the City's transfers to CPS.

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Debt Service Fund

Debt service payments are expected to rise by $2.9 million in FY 2017 to $42.3 million. While debt payments on older debt are declining, we anticipate the issuance of new bonds for City and school projects in April or May 2016. The FY 2017 budget includes an $8.5 million provision to address debt service requirements for the new debt issues. Listed below are the debt funding sources for FY 2017:

City General Fund – pre-lockbox debt	$ 6,446,005
Debt Service Fund Balance – pre-lockbox debt	4,205,000
City lockbox	6,019,699
School lockbox	13,698,576
Spring 2017 debt issues – city and school lockboxes	8,500,000
South Norfolk TIF	600,023
Greenbrier TIF	1,471,738
Federal subsidies	890,011
Other sources	470,469
Total sources of debt payments	$ 42,301,521

Since 2004, the City has designated certain revenue for capital lockboxes that support financing of school and City capital projects. Debt service on all debt issued after 2003 is paid from the designated revenues. During FY 2017, pre-lockbox debt payments decline by $5.6 million while debt payments funded with locked revenues increase by $8.5 million.

At June 30, 2015, the Debt Service Fund (DSF) balance was $24.0 million which the City plans to use for future debt payments. The FY 2016 and 2017 budgets draw $4.5 million and $4.1 million respectively from the available fund balance in order to pay pre-lockbox debt. The City will continue utilizing the DSF fund balance until pre-lockbox debt is entirely retired (FY 2024); at which point, the DSF fund balance will be depleted.

Virginia Public Assistance Fund (Social Services)

The Social Services Division of Human Services is the local agency that administers federal and state public assistance programs. Social Services' primary function is to determine the eligibility of local residents for a variety of federal and state social benefit programs. The Social Services budget is dropping slightly from $21.6 million in FY 2016 to $21.3 million in FY 2017, a decrease of $350,000 (1.6%). The primary factors impacting the VPA budget are:

• Employee compensation – 2.5% pay raise	$ 323,300
• Reduction in OPEB costs	(452,500)
• Reduction in retirement costs	(213,600)
• Employee turnover and other savings	(129,200)
• Increases in general and administrative costs	122,000

No changes in the division's level of services are planned for FY 2017. The proposed funding level is adequate to meet state and federal mandates for the programs it administers.

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Chesapeake Integrated Behavioral Healthcare:

Chesapeake Integrated Behavioral Healthcare (CIBH) was established as a community services board to provide mental health, development, and substance abuse services in accordance with Virginia statute. These services are provided through CIBH, the agency that reports to a local board appointed by City Council. The FY 2017 operating budget for CIBH is proposed to increase by $1.59 million (7.0%) to $24.5 million. Much of the increased funding is needed to add staff and is related to statewide efforts to improve mental health. A complete listing of new positions starts on page B-28. A summary of significant changes in the CIBH budget is noted below:

• New positions to address mental health	$ 957,300
• Employee compensation – 2.5% pay raise	341,000
• Reduction in OPEB costs	(436,000)
• Reduction in retirement costs	(223,700)
• Employee turnover and other changes	205,600
• Increase in tele-psychiatry costs	300,000
• Increase in public assistance payments	309,000
• Increases in general and administrative costs	137,000

Tax Increment Funds (TIF)

The statutes governing TIFs allow for the transfer of surplus TIF funds to the General Fund. In accordance with past practice, this budget includes provisions to transfer surplus funds from both the South Norfolk and Greenbrier TIF Funds to the General Fund in order to address maintenance cost of projects funded by the TIFs and other costs that are directly related to the TIF districts. We recommend the transfer of $293,660 of surplus funds from the Greenbrier TIF to the General Fund to fund the maintenance of improvements to the district and to fund the Police Department Hotel Interdiction Program. We also recommend the transfer of $115,700 from the South Norfolk TIF to fund the maintenance of improvements to that district along with the cost of the Sheriff's work crew assigned to South Norfolk.

In addition to transfers of TIF resources for the maintenance of TIF improvements and related costs, we also transfer $1 million annually from the South Norfolk TIF to the General Fund to pay a portion of the debt service costs related to the renovation of Oscar Smith Middle School. Ten annual transfers were planned for the OSMS renovation; the transfers are scheduled to end in FY 2021.

Starting in FY 2016, the City declared a surplus in the Greenbrier TIF and transferred $2 million to the General Fund that supports operations of the City and Schools. The additional funds help Chesapeake Public Schools address the recruitment and retention of teachers as well as increasing employee health insurance. The City's share of surplus TIF funds helps address existing commitments to residents and employees. We recommend a continuation of the annual $2 million surplus declaration in support of CPS and City operations.

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Public Utility Fund

In February 2013, the City Council approved a plan to increase water and sewer rates by 4.9% in each of the next several years. The FY 2017 operating and capital budgets include the fourth scheduled rate increase starting July 1, 2016.

Utility expenditures reflect a continuation of current service levels with an allowance for modest growth as new residential and commercial properties are built. Spending by Public Utilities is expected to grow by $1.4 million, rising from $64.3 million in FY 2016 to $65.7 million in FY 2017. The primary factors affecting the Utility budget are as follows:

• Increased routine capital costs (small improvements and replacements)	$ 2,196,700
• Add nine (9) new positions: two (2) motor equipment operators, one (1) utility electronics technician, one (1) water meter technician, one (1) water treatment plant operator, two (2) customer service clerks, one (1) cross connection supervisor, and one (1) project manager	510,000
• Employee pay raises (2.5%)	274,100
• Increased overhead (General Fund cost allocation)	250,000
• Decreased contract costs of purchased water	(314,000)
• Decrease in debt service costs (principal and interest payments)	(817,900)
• Decrease in other post-employment benefits (OPEB)	(448,400)
• Decrease in retirement costs	(134,000)
• Other changes in salaries and benefits (primarily vacancy savings)	(383,000)
• Other changes in cost of general operations	287,100

The proposed budget increase will allow the department to improve its response to citizen requests, improve maintenance and dependability of the water and sewer systems, and improve department productivity.

Stormwater Management Fund

The Stormwater Management Operating Budget is proposed to decline by $3.9 million, dropping from $14.6 million in FY 2016 to $10.6 million in FY 2017. Significant changes to the Stormwater budget are noted below:

• Remove one-time equipment purchases during FY 2016	$ (2,761,000)
• Add one (1) office assistant needed for compliance reporting	40,400
• Increase in overhead allocation (offset by OPEB reduction, below)	130,000
• Employee pay raises	114,700
• Reduction in OPEB and retirement expenditures	(236,600)
• Other changes in salaries and benefits (primarily vacancy savings)	(288,200)
• Reduction in purchased services, including cave-in repairs	(829,600)
• Net reduction in general operations	(98,300)

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Chesapeake Transportation System Fund (toll roads):

The Chesapeake Transportation System (CTS) includes the tolled section of Route 168 and a section of Dominion Boulevard (Route 17) that is in the final stages of construction. Completion of Dominion Boulevard is contractually required by April, 2017. However, construction is currently ahead of schedule and the project could be finished by the late fall or winter of 2016. The Operating Budget for CTS increases from $5.3 million for FY 2016 to $19.8 million in FY 2017 and includes:

• Dominion Boulevard toll operational costs subsequent to construction phase	$ 4,471,000
• Increase in debt service costs (mostly related to Dominion Boulevard)	9,965,000
• Decrease in personal service costs for Expressway, net of pay raises	(169,600)
• Increase in renewal and replacement costs (corrects FY 2016 omission)	773,000
• Reduction in other Expressway operating costs	(567,900)

As part of financing Dominion Boulevard several years ago, we also borrowed money to refund the existing senior debt on the Expressway. This allowed the Expressway to take advantage of more favorable interest rates. Under terms of the new bonds, all principal payments for both Routes 168 and 17 were deferred for four years while the new road was under construction. A substantial portion of the new project is also funded from a $152 million subordinate loan from the Virginia Transportation Infrastructure Bank (VTIB). Under the agreement with VTIB, payments for subordinate Expressway debt held by the Commonwealth of Virginia and the City of Chesapeake are also deferred until two years after construction is complete (interest costs accrue during the entire period the loan is outstanding). The operating budget includes all accrued interest, but only principal payments that are due and payable.

Tolls on Dominion Boulevard will start fifteen (15) days after road construction is complete. Principal payments for senior bond holders will start July 2018. Principal payments for subordinate debt owed to VTIB are expected to start July 2019.

Tolls on the Chesapeake Expressway are adjusted periodically in order to ensure adequate funding for the road's operational and maintenance costs and to meet the City's debt obligation. The next scheduled increase occurs May 1, 2016; the FY 2017 budget reflects increased toll revenue related to the rate increase.

Risk Management Fund

The Risk Management Fund operates as an internal service fund providing insurance and worker compensation services to other City departments. The Risk Management Fund increases by $864,268 from $8.5 million in FY 2016 to $9.4 million in FY 2017. Practically all of the increased costs are related to expected increases in property and casualty insurance and to rising worker compensation costs.

Other City Operating Funds

The proposed operating budget also includes several other funds whose spending levels are not changing significantly from FY 2016. Separate funds are maintained for the following purposes:

- Interagency Consortium – operates as a division of Human Services to provide services to students with disabilities. City staff work closely with Chesapeake Public Schools and other human service agencies to address educational and behavioral needs of eligible students. Proposed annual budget - $3.7 million.

- Fee-Supported Programs – this fund is used to account for activity of several services that are supported entirely by fees. Three services are currently included in the fund:
  - Fire Department's Hazardous Environmental Action Team (HEAT) focuses on the reduction and elimination of dangers caused by hazardous materials and conditions. Funding of the program is provided by inspection fees and fines issued for violations.
  - Police Department's Red Light Photo-Enforcement project monitors intersections with higher than average accident rates. The program is funded by fees collected from offenders identified by the contractor maintained cameras.
  - Development & Permit's Code Compliance/Demolition Program seeks to remove nuisance buildings and conditions that exist in residential and commercial areas. Funding is derived from property owners via liens attached to offending properties.

  Proposed annual budget - $0.9 million.
- Conference Center and Tourism – operates the Chesapeake Conference Center and the City's Tourism Bureau, both of which are funded from dedicated meals and lodging taxes. Proposed annual budget - $4.0 million.
- E-911 – operates as a division of the Police Department and to answer emergency (911) calls and to dispatch appropriate fire, emergency medical, and/or police personnel to assist citizens. Proposed annual budget - $6.2 million.
- Juvenile Services – provides safe and secure detention services for juvenile offenders. Proposed annual budget - $6.8 million.
- Central Fleet – operates as an internal service fund to provide vehicle maintenance services to other City departments. Central Fleet also sells fuel to Chesapeake Public Schools at prices tied to delivery costs. In addition to fleet and garage services, the fund is also used to account for activity of the Sheriff's work crews that provide services to Public Works and Parks, Recreation & Tourism. Proposed annual budget - $15.5 million.
- Information Technology – operates as an internal service fund to provide technology and related services to other City departments and Chesapeake Public Schools. Proposed annual budget - $9.8 million.
- Mosquito Control Commission – operates as an autonomous unit governed by a commission appointed by City Council. Its purpose is to control mosquito populations and prevent mosquito borne illnesses. Proposed annual budget - $4.4 million.

Concludes on next page.

Conclusion

This spending plan balances existing revenue and other resources with overall service demands and other needs. No changes are proposed in general tax rates and only modest fee increases are proposed. The FY 2017 Proposed Operating Budget honors our commitment to Chesapeake Public Schools while also addressing retention, recruitment, and health care costs of city employees.

In the coming weeks we will schedule work sessions for Council to review this proposed budget in light of sustainability. The City staff remains committed to providing quality public services. While recommending a prudent spending plan that protects the City's financial position, we also propose strategically adding resources in areas that have been underfunded or face new demands.

I am confident that the strategies recommended in this proposed budget meet most citizen expectations for quality levels of community services while also sustaining the City's strong financial position. I look forward to working with the entire City Council in the coming weeks as you review this proposal and adopt a budget plan that meets current and future needs of Chesapeake citizens.

Sincerely,

James E. Baker
City Manager