MEMORANDUM

Date: April 30, 2015

To: The Honorable Chair and Members
Pima County Board of Supervisors

From: C.H. Huckelberry
County Administrator

Re: **Transmittal of the Recommended Fiscal Year 2015/16 Budget**

Introduction

This memorandum transmits the Recommended Fiscal Year (FY) 2015/16 Budget for Pima County. These recommendations are made based on information available in April 2015. It is possible additional relevant information will become available for the Board of Supervisors as it deliberates on the budget prior to final adoption on June 16, 2015.

On March 17, 2015, the Board ordered five additional public hearings be held on the budget. Three of these hearings have been completed, and two will occur after this budget transmittal memorandum is released. In total, the Board will have held seven public hearings regarding the budget, totaling approximately 20 hours, before Final Budget Adoption. The budget hearings have been televised, as well as available for viewing through the internet.

All budget documents, as submitted by County departments, have been available on the County's website since February 2, 2015. Over 30 budget-related communications have been issued to the Board during FY 2015, and these are available for review at http://webcms.pima.gov/government/county_administrator/.

Significant dates in the budget adoption and tax levy processes are as follows:

May 5, 2015	Board of Supervisors Budget Hearing
May 12, 2015	Board of Supervisors Budget Hearing
May 12, 2015	Board of Supervisors Recommended Budget Hearing
May 19, 2015	Tentative Budget Adoption (Sets Budget Ceiling)
June 16, 2015	Truth in Taxation Hearing
June 16, 2015	Final Budget Adoption
August 17, 2015	Tax Levy Adoption (Date Set by State Statute)

Following this budget memorandum are:

- Budget schedules showing fund balances, expenditures, revenues, transfers and other financing sources.
- A summary of each department's budget, including a description of the budget on a line-item account basis.
- Descriptions of all supplemental funding packages requested by each department.

The County's base operating budget for all funds set forth in this recommendation includes projected continuing and new cost shifts, revenue reductions and revenue sharing.

TABLE OF CONTENTS

I. OVERVIEW OF RECOMMENDED BUDGET

The FY 2015/16 Recommended Budget is based largely on the County's response to a set of unique challenges from a variety of outside sources. These challenges include increased retirement, employee health benefit and other costs that are not under the control of the County. In addition, the Arizona Legislature and the Governor balanced the State Budget by transferring $23.2 million of FY 2015/16 State budget costs to Pima County. Up to $18.6 million of these cost shifts are in dispute and will likely result in litigation. These additional costs imposed by the State cause significant uncertainties in the development of the County budget and have significant impacts on all of Pima County's existing service priorities and programs, including law enforcement, healthcare and economic development.

Like all governments in Arizona, Pima County has necessarily adjusted to reduced revenues and increased service demands during the economic recession. More than seven years ago, at the beginning of the recession, Pima County began taking actions in response to declining resources and an increasingly uncertain operating environment. Numerous initiatives were developed and implemented to address redundancy and improve efficiency. Internal services were centralized to increase efficiency and reduce cost. The workforce was reduced, primarily through normal attrition. Priorities were re-evaluated and items of discretionary spending, such as travel, have been nearly eliminated. Department and agency budgets have been incrementally reduced over time through a managed, thoughtful process.

The cumulative effect of these departmental budget reductions has been substantial. General Fund supported departments have been reduced 11.5 percent, except the Sheriff's Office, which was reduced only 2.5 percent. In addition to these reductions, departments were required to absorb the impact of salary increases awarded by the Board of Supervisors in FY 2015. This is equivalent to a 0.7 percent reduction. Departments also have not received additional resources to address inflationary increases to operational costs or the steady decline of federal and state special and grant revenues that have historically supplemented their core services. The result over time is that departments have been unable to reinvest in the programmatic infrastructure to support their functions. The FY 2015/16 transfer of additional State budget costs exacerbates this problem.

Between FY 2010 and FY 2014, primary property taxes levied by the Board of Supervisors decreased 7 percent, or an aggregate of $20.6 million, over that four-year period. In FY 2010, the primary property tax levy was $298 million. The levy declined to $277 million in FY 2014. At the same time, the General Fund balance declined from $77.5 million to $42.9 million. These numbers reflected Pima County's long-term strategy of decreasing the fund balance without raising property taxes to assist the local economy in recovering from the Great Recession. In FY 2015, the General Fund balance had been reduced to the minimum desirable, and a property tax rate increase was required by the Board to bring the budget into structural balance with expenditures.

For the first time in several years, the primary property tax base in Pima County will increase in FY 2015/16 by 1.36 percent. It is expected that the property tax base will continue to increase modestly for the next few years.

The current primary property tax rate of $4.2779 is unfortunately recommended to be increased $0.1098 (due to State cost transfers). This recommended increase in the primary property tax rate will produce $8.1 million more in revenue than the current rate, but $55.3 million less than the Constitutional Levy Limit, which is indexed for inflation. These additional property tax revenues from the increased rate are recommended to offset $8.1 million of State cost shifts to Pima County. The remaining $4.7 million to as much as $15.1 million of State cost shifts have been or will be absorbed within the FY 2015/16 budget.

It is recommended that the combined secondary property tax rates be increased by a net $0.0700. The Library District and Flood Control District rates are recommended to increase by $0.0600 and $0.0100 respectively to address increases in operational costs during the last several years of declining revenues. The Debt Service rate is recommended to be unchanged.

Combined with the recommended increase of $0.1098 in the primary tax rate, the combined recommended County property tax rate is $5.8965, or $0.1798 more than the current year. The combined County property tax levy is $447,130,181, or $19,151,357 more than the current year.

The recommended combined total County Budget for FY 2015/16 is $1,164,953,662, which is $23,510,590, or 1.98 percent, less than the current year's Adopted Budget. This will be the fourth consecutive year the County budget has decreased.

- The projected General Fund available ending balance for FY 2015 is $31,847,551, an increase of $14,373,071 over the budgeted General Fund Reserve of $17,474,480. This amount represents the beginning fund balance for FY 2015/16.

- It is recommended that the non-recurring FY 2015 ending balance be allocated for the following purposes:

  - $12,500,000 to fund the contract payment to Banner Health on behalf of the Banner–University of Arizona Medical Center South Campus. This represents a one-time $2.5 million reduction to offset a portion of the FY 2015/16 State cost shifts to Pima County.

  - $19,347,551 to fund a portion of the total General Fund Reserve for FY 2015/16 of $32,849,201, which is 6 percent of General Fund revenues. The reserve has been increased to accommodate a worst-case scenario of State budget cost shifts being $23,200,000. If this reserve is not spent, it will represent the base ending fund balance for FY 2015/16.

- Assuming continuation of the current primary property tax rate of 4.2779, General Fund base revenues and transfers-in for FY 2015/16 are projected to be $542,550,218, which is $12,738,453, or 2.4 percent, more than the current year.

- Excluding primary property taxes, General Government revenues from all other sources are projected to increase $5,008,369, or 3.12 percent.

- The value of the net primary property tax base is projected to increase 1.36 percent, which will result in an increase in the primary levy of $4,358,277 at the current tax rate.

- Total primary property tax revenues from all sources are projected to increase $3,526,291 at the current tax rate. Primary property tax revenues are different than the tax levy due to the impact of tax collection and delinquent tax collection rates and associated penalties and interest.

- General Fund base expenditures and transfers-out for FY 2015/16 are projected to be $543,183,680, which is $19,102,565, or 3.4 percent, less than the current year.

- General Fund base expenditures exceed base revenues by $633,462.

- State cost transfers to Pima County presently enacted into law will impact recommended budget expenditures by as much as $23,200,000. When added to the existing State budget cost transfer, this is an annual budget impact of $106 million for FY 2015/16, or 33 percent of the existing primary property tax rate of $4.2779.

- To accommodate a portion of State cost transfers, the Recommended Budget includes an additional two-percent reduction in expenditures for County departments in all funds. Expenditures are decreased $6,970,363 in the General Fund and $10,870,561 in the overall County Recommended Budget.

- The General Fund Budget Reserve totals $32,849,201.

- It is recommended that the primary property tax rate be increased by 10.98 cents to a total rate of $4.3877 to fund $8.1 of the $23.2 million of FY 2015/16 State budget cost transfers that cannot be accommodated by internal budget reductions or increases in ending fund balances for the General Fund.

- The Recommended Budget for the Library District is $40,166,950, a $2,394,097 increase from the current year; and the tax rate is recommended to increase 6 cents to $0.4953.

- The Recommended Budget for Debt Service is $110,820,702, a $4,133,120 decrease from the current year; and the tax rate is recommended to remain unchanged at $0.7000.

- The recommended operating budget for the Regional Flood Control District is $17,490,112, an increase of $393,384 from the current year, and the tax rate is recommended to increase 1 cent to $0.3135.

- The combined, total recommended County property tax rate is $5.8965, a $0.1798 increase from the current year; and the resulting combined County levy is $447,130,181, a $19,151,357 increase from the current year.

- The combined, total Recommended County Budget for FY 2015/16 is $1,164,953,662, which is 23,510,590, or 1.98 percent, less than the current year.

II. STATE BUDGET COST SHIFTS

A. Overview of State Cost Shifts

Prior to a discussion of the Pima County Recommended Budget, a review of the State of Arizona's shifting of budget costs to Pima County is necessary; as these shifts have direct, adverse impacts on the programs and services provided by the County for FY 2015/16.

Over the years, the State has adopted new programs, paid for them entirely for one or two years, and then shifted the program costs to the counties. Examples are the Restoration to Competency and Sexually Violent Persons programs. Restoration to Competency takes a criminal defendant who would otherwise be declared incompetent to stand trial and improves their mental competency where they are able to stand trial. Sexually Violent Persons are individuals confined to the State Prison System who, upon completion of their sentence, are deemed to be a continuing threat to public safety and are confined at the Arizona State Hospital. Both of these programs were initially paid entirely by the State. They are, without question, State programs and should be entirely paid for by the State. Now, however, their costs have been entirely or partially shifted to the counties. The same is true for the State Indigent Health Program (Arizona Health Care Cost Containment System, Arizona Long Term Care System and Behavioral Health System). These ongoing State cost transfers to Pima County, including the County's share of salaries and benefits for the courts, totaled $82.8 million, or 26 percent of the County's primary property tax rate last year.

In balancing the State Budget this year, the Governor and Legislature have accelerated cost transfers to the counties and increased the cost transfer to Pima County by more than any other county in the State. The proposed new cost transfers to the County presently enacted into law equal up to $23.2 million and are shown in Table 1 below.

Table 1: New FY 2015/16 State Cost Transfers to Pima County.

Description	Amount Required From Pima County
State Juvenile Corrections	$ 1,840,289
"Additional State Aid for Education"	From $8.1 to $18.6 million*
Restoration of ALTCS Dental	141,000
AZDOR Operating Cost	1,514,775
2016 Presidential Preference Election (Net)	1,100,000
Total	Up to $23.2 million

**The legislation creating this shift is so poorly drafted, and delegates so much discretion for allocations to the Property Tax Oversight Commission, it is impossible to know the exact final amount of this cost shift.*

When these new increased State budget cost transfers are added to last year's transfers, the total is $106 million for FY 2015/16, or nearly 33 percent of the existing primary property tax rate of $4.2779. The County is clearly subsidizing the State.

These budget transfers from the State will necessitate changes in the funding of programs and services contained in this Recommended Budget. A partial list of impacts of these transfers to the General Fund Recommended Budget unfortunately includes:

- A two-percent, across-the-board reduction of $6,970,364 in General Fund expenditures.
- A $5,000,000 reduction in funding available for the Pavement Preservation Program.
- A $2,500,000 decrease in the annual payment under the existing contract for the Banner-University Medical Center South Campus.

These reductions will directly impact the level of services Pima County will be able to provide to our residents in FY 2015/16.

B. School Funding and the One-percent Cap on Residential Primary Property Taxes

In 1980, 35 years ago, Arizona voters approved a constitutional limit on the amount of primary property tax that can be levied on residential property. The aggregate amount of primary property taxes payable to jurisdictions on residential property cannot exceed one percent of the property's value. The Legislature, in 1981, as part of its effort to equalize school funding and satisfy its constitutional obligation to provide for a uniform statewide school system, provided that school district levies would be reduced when the one percent cap is exceeded, and the State would provide additional funding to the impacted school district to make up the difference. This has been the law and practice for 34 years.

Suddenly, the Legislature and the Governor have shifted responsibility for most of this additional school funding from the State to the local taxing jurisdictions. This has allowed the State to increase its revenues while ostensibly not raising taxes; instead forcing local jurisdictions to raise their taxes to cover the State's obligations. And they did this without the two thirds super majority required under the State Constitution for passage of measures that raise State revenues. Ironically, for Pima County, which is funded with property taxes, this just exacerbates the problem with this legislation. The legislation delegates an enormous amount of discretion to the State's Property Tax Oversight Commission to determine how much of the required school funding will be provided by which jurisdictions. Therefore, the actual cost to Pima County will not be known until the Commission meets in September 2015 – after the property tax rate and levy have been adopted. This lack of clarity creates a great deal of uncertainty in the County budget.

Property taxes are constitutionally required to be levied for a particular purpose. For Pima County, the purpose has been the general support of the County government. Now, a portion of the County's tax levy will really be used for the general support of one or more other taxing jurisdictions (school districts), but it is impossible to determine, at this point, the amount of this support.

It is estimated, based on the Governor's budget documents, that Pima County's primary property taxing entities will be required to pay up to $18.6 million to the Tucson Unified School District and smaller amounts to other school districts that have qualifying residential properties. Our estimated share of these payments ranges from $8.1 million up to the full amount of $18.6 million. Given the level of uncertainty, I will recommend the County increase the primary property tax rate by $0.1098, which is sufficient to offset the lower estimate of $8.1 million. I will also recommend the County increase the General Fund Budget Reserve, in part to have sufficient contingency funds to cover the worst-case estimate of $18.6 million. This increase in the budget reserve will come from other parts of the County's General Fund budget.

III. GENERAL FUND ENDING FUND BALANCE: FY 2015

A. <u>Positive Ending Fund Balance</u>

The recommended General Fund ending balance for FY 2015 is $31,847,551. This is a projected increase of $14,373,071 over the budgeted General Fund Reserve of $17,474,480. This ending balance represents approximately 6 percent of projected revenues for FY 2015 compared to the ending fund balance of 3.6 percent last year.

This net increase of $14,373,071 results from numerous offsetting increases and decreases in actual expenditures, revenues, and operating transfers from the Adopted Budget, including:

- A $10.4 million greater beginning General Fund balance than was anticipated at the time the FY 2015 Budget was adopted. Several departments experienced larger cost savings than anticipated, such as $2 million in mandated long-term care payments, elections and general facilities-related costs. Partially offsetting these savings were overspending in the Sheriff's Office and Indigent Criminal Defense.

- A $2 million savings associated with the freeze of unexpended Pavement Preservation Funds as a budget control measure in response to State budget cost shifts. Three million dollars of the original $5 million allocation for this purpose was spent.

- The forecasted FY 2015 ending fund balance also includes savings in costs associated with inmate health of $2 million and various general government services departments.

B. Recommended Uses of General Fund Ending Balance

Set forth below are my recommendations for use of the $31,847,551 of nonrecurring, one-time resources projected as the available ending balance of the General Fund on June 30, 2015.

1. Banner–University of Arizona Medical Center South Campus

Over the past several years, the partnership between Pima County, The University of Arizona and now Banner Health has allowed the hospital and Pima County to align incentives and expand opportunities within the academic medical system.

Beginning in 2010, the County entered into a two-year agreement with the Arizona Board of Regents on behalf of The University of Arizona College of Medicine for funding of The University of Arizona Medical Center South Campus. In May 2012, a second two-year contract was approved, providing for annual base funding at $15,000,000 in consideration for a variety of services being provided at the South Campus complex that will benefit the County and health of its residents. A third two year contract became effective July 1, 2014. This contract was assumed by Banner Health upon its merger with the University health system.

Some have criticized our property tax commitment to the academic medical system. This support has been $15 million per year for the last few years, which is far less than the $34 million Pima County lost when it last operated the hospital in 2004. This arrangement, where a professional hospital nonprofit, Banner Health, together with the academic medical college of The University of Arizona, operates our hospital, is a good value for Pima County taxpayers as compared to the property tax support being provided to the Maricopa County hospital system by Maricopa County taxpayers.

In 2005, funding of the Maricopa County hospital was made a separate secondary property tax special district, the Maricopa Integrated Health System. Since then, its property tax support from Maricopa County property taxpayers has totaled over $531 million. This year, it is $65.1 million. In addition, a significant portion of the correctional medical costs in Maricopa County of $61.4 million per year are funneled to the Maricopa Integrated Health System; hence, the property tax support on a per capita basis provided by a Maricopa County resident is far more than the property tax support of a Pima County resident for our hospital system.

This hospital arrangement has my full support; but given the significant State cost transfers, I recommend a one-time reduction in the FY 2015/16 payment to Banner Health be reduced from $15,000,000 to $12,500,000 to offset a portion of the State budget cost shifts.

2. General Fund Reserve

In Fiscal Year 1997, the General Fund Reserve was budgeted at zero. Since that time, the Board has taken a variety of significant actions to stabilize finances and enhance the fiscal integrity of the County. This has enabled the Reserve Fund to be steadily restored.

The Government Finance Officers Association recommends, as a minimum benchmark, that 5 percent of operating revenues be set aside as fund balance. For most of the past 7 years, the Board has been able to achieve or exceed a 5 percent reserve within the Adopted Budget. The exception was this fiscal year, when the reserve was nearly 4 percent.

The budget reserve has contributed to an enhanced bond rating being assigned to the County, which has saved approximately $2 million annually in reduced interest payments on County bond projects. The reserve has also enabled the County to sustain the negative fiscal impacts of a variety of unforeseen events over which the County has had little or no control.

The persistently weak economy has put the County in an increasingly uncertain operating environment. The primary tax base began contracting in FY 2011 and declined 7.04 percent in FY 2012, 2.84 percent in FY 2013, 6.38 percent in FY 2014 and 0.54 percent in FY 2015. The property tax base will end its decline in FY 2015/16 and will increase by a modest 1.36 percent. It is anticipated the real estate market and construction industry in the County will take several more years to fully recover. In addition, actions of the State and Federal governments that financially impact the County have become increasingly more common, erratic and unpredictable. The trend has been and continues to be shifting program funding to local governments. Consequently, maintaining the Reserve Fund balance at an adequate level has become an important goal.

After the appropriation recommended above to fund the County's agreement regarding Banner-University Medical Center South Campus, the amount remaining of the projected FY 2015 General Fund ending balance is $19,347,551, which I recommend be allocated entirely to fund a portion of the General Fund Reserve.

3. Summary of Recommended Uses of General Fund Ending Balance

Table 2 below summarizes the recommendations discussed above for allocation of the nonrecurring, one-time resources projected as the FY 2015 available ending fund balance of $31,847,551.

Table 2: Recommended Allocation of FY 2015 General Fund Ending Balance.

Recommendation	Amount
Banner–University Medical Center South Campus	$12,500,000
General Fund Reserve	19,347,551
TOTAL	**$31,847,551**

IV. GENERAL FUND BASE BUDGET: FY 2015/16

A. General Fund Base Budget Revenues

Assuming continuation of the current primary property tax rate of $4.2779, projected FY 2015/16 base budget revenues and operating transfers to the General Fund total $542,550,218. This is a $12,738,453, or 2.4 percent, increase from the current year budgeted revenues and operating transfers to the General Fund.

Below is a brief discussion of each category of projected General Fund base revenues.

1. General Government Revenues Other Than Property Taxes

Excluding primary property tax revenues, projected FY 2015/16 base budget General Government revenues from all other sources is $165,449,838; which is a $5,008,369, or 3.12 percent, increase from the current Adopted Budget.

The largest revenue stream in this category, state shared sales tax, is projected to increase by $1,860,000, or 1.74 percent, to $108,500,000; reflecting a slow but continued recovery in the local economy. Vehicle License Tax revenue is also projected to show continued improvement next year with an overall increase of $1,500,000, or 6.22 percent.

2. Primary Property Tax Revenues

Annual 5-Percent Cap on Taxable Net Assessed Value Increases

FY 2015/16 represents the first effective year of a Constitutional amendment, approved by Arizona voters two years ago, that will substantially limit future overall appreciation of the existing property tax base by setting a 5 percent cap on taxable net assessed value increases from year to year. Previously, the market dictated increases in taxable net assessed value.

Primary Property Tax Revenues

The Taxable Assessed Value for FY 2015/16 totals $7,620,360,873. This is a net $101,878,885, or 1.36 percent, increase over the current year and represents the first annual increase in Taxable Assessed Value since FY 2010. While this amount represents an increase from FY 2015, the Taxable Net Assessed Value is still $1,365,350,957, or 15.2 percent, less than six years ago in FY 2010. Next fiscal year, the market value of existing property in the County will decrease by 0.57 percent; however, this will be partially offset by an increase of 1.93 percent as a result of new construction added to the tax base. Because the primary tax base will increase next year, use of the current year's tax rate will result in a levy amount that is 1.36 percent greater than the current year's levy.

Assuming the same primary rate as this year of $4.2779 per $100 of taxable assessed value, the resulting primary levy is $325,991,418. This is $4,358,277 more than the amount levied in this year's Adopted Budget.

In addition to collection of current year property taxes, the County receives revenue from the payment of delinquent property taxes from prior years and associated interest and penalties. Together with the projected primary property tax collection next year, assuming continuation of the existing rate of $4.2779, the total base property tax revenues projected for FY 2015/16 are $329,255,534. This amount is $3,526,291, or 1.08 percent, more than the total primary property tax revenues adopted in this year's Budget. The majority of the difference between the levy amount and the revenues collected is attributable to the overall collection rate and reductions in the forecasted collections of penalties and interest on delinquent property tax collections.

State Truth in Taxation statutes determine the County's revenue neutral primary property tax levy each year. A neutral levy and corresponding tax rate is defined as the previous year's levy plus additions to the tax base from new construction. The County would have to further increase the primary property tax rate in order to reach a neutral levy. Pursuant to statute, the County's neutral primary rate is $4.3025, or $0.0246 higher than the current year's rate. The resulting neutral primary levy is $327,866,027, or 0.508 percent, greater than the levy produced by the current year's rate.

This statutory benchmark is more restrictive than the County's Levy Limit imposed by the Arizona Constitution, which is indexed to reflect a modest annual rate of inflation of 2 percent. The Primary Levy Limit imposed by the Arizona Constitution allows the County's primary rate to be increased to $5.1006, or $0.8227 higher than the current year's rate. The resulting constitutionally capped levy is $388,684,128, which is $62,692,710, or 19.2 percent, greater than the levy produced by the current rate.

3. Departmental Revenues

Base budget General Fund revenues from departments and operating transfers-in for FY 2015 are projected to be $47,844,848. This is a $7,203,792 net increase over the current year's budget.

This increase reflects improvement in local economic activity and the corresponding utilization of County services for fees. Increases in revenues range from additional Correctional Housing Fees collected by the Sheriff from various jurisdictions utilizing jail facilities to facilities rents and increases in operating transfers-in from various County funds. Despite departmental revenues and operating transfers-in increasing in FY 2015/16, they are still $26,411,066 less than eight years ago when the economic recession began.

B. General Fund Base Budget Expenditures

The amount required to fund General Fund-supported base budgets for both departmental expenditures and transfers-out is $543,183,680; which is $19,102,565, or 3.4 percent, less than the current year's base budget. This base expenditure amount represents adopted departmental budgets adjusted for new or amended federal- and state-mandated expenditures; recurring supplemental requests, annualized as appropriate, that were adopted in the current year's budget; impacts to base pursuant to Board-adopted budget policies and prior directives; and decreases for one-time expenditures in the current year. Expenditures also include the allocation of the nine decision packages approved by the Board in FY 2015 to the respective impacted departments and funds.

Since the economic recession began more than seven years ago, a series of across-the-board reductions in departmental budgets have been implemented. The cumulative reduction in departmental budgets during this time has been approximately 11.5 percent, except the Sheriff's Office, which has been reduced by 2.5 percent. Even after the mandated and inflationary cost increases experienced by the County over the last seven years, General Fund base expenditures are currently less than they were in FY 2009.

Significant components within recommended base budget expenditures include (before adjustment for Final Budget Recommendations):

- $279,447,079, or 55 percent, of General Fund expenditures for Justice and Law Enforcement functions.
- $66,046,970 for mandated payments to fund State programs for indigent acute and long-term healthcare, as well as mental healthcare.
- $13,116,468 for adult and juvenile detention healthcare.

- $95,526,744 for General Fund employee benefits, including medical, dental and life insurance and contributions to the four separate State retirement systems in which various employee groups and officials participate.
- $744,994 in the Board of Supervisors Contingency Fund; the same amount appropriated in the current year's budget.
- $4,383,041 for allocation to Outside Agencies.

Significant additions to General Fund base expenditures for FY 2015/16 include:

- $5,950,835 to fund the cost of the 2015/16 Bond, Presidential Preference Primary and other elections.
- $4,804,843 ongoing increase in the Public Safety Personnel Retirement System contribution. The Board approved assuming the full annual cost of an adjustment required due to a negative court decision regarding benefits for retired employees.
- $4,100,000 to fund the one-time costs to complete an upgrade next fiscal year of the County's enterprise level financial systems.
- $1,121,814 to annualize funding required for the maintenance of the County's new Public Service Center Facility.
- $548,654 to fund increases to General Fund support to Health Services and Pima Animal Care approved by the Board.

Information Technology Initiatives

In August 2014, the County began a new Information Technology (IT) initiative to lease computers rather than purchase them as the County had historically done. At that time, there was no countywide standard for when to replace aging computers, with some departments replacing IT equipment every four or five years and some not replacing the equipment for much longer periods. To bring uniformity to the County, the Board approved the concept of leasing computer devices on a three-year renewal basis. Current budget constraints make continued implementation of this initiative difficult.

The IT Department is analyzing several models of equipment replacement so I may provide the Board with options to allocate the very limited resources the County has for this initiative. Those options include a return to purchasing IT equipment, using different lease terms for leasing equipment, and a combination of leasing and purchasing based on the greatest needs for security and capability for IT equipment, department by department. I expect to be able to make a recommendation to the Board at the time of the Tentative Budget hearing.

C. Change in the Process of Budgeting for Vacant Positions

Beginning with the FY 2015/16 budget, the County has made a significant change in the way it handles vacant positions and the turnover of staff within the budget. In the past, a department was allowed to budget for a certain number of vacant positions based on an estimated staff turnover rate. The associated salaries and benefits costs for these positions were offset by budgeting a vacancy savings or attrition offset or factor. While this method of budgeting did not impact the bottom line of the departmental budget, it did tend to overstate the number of budgeted positions (FTEs) in the overall County budget. Having a larger than required pool of positions also meant additional costs to the County when benefits and other position-related adjustments were made to departmental budgets. In essence, for every $1 in salary, $0.34 in benefits was budgeted, allowing departments and agencies to spend funds for unbudgeted projects or programs. The cost impacts of budgeting excess positions that would not be filled during the fiscal year are significant and outstrip the benefits of having a ready pool of positions available as funding becomes available or staffing needs change; thus, the decision to no longer utilize a vacancy savings object to offset excess position costs.

As the result of this change in the budgeting of vacancy savings, combined with other position-related adjustments, the County's workforce has decreased by 261 FTEs from the FY 2015 budget. Since FY 2008, the workforce, countywide, has been reduced by 1,402 FTEs, or 16.7 percent, as shown in Table 3 below.

Table 3: Total Budgeted FTE Positions, FY 2008 Adopted Budget through FY 2015/16 Recommended Budget

FY	Budgeted FTEs	Change in Budgeted FTEs	Cumulative Change in Budgeted FTEs
2007/08	8,396		
2008/09	8,113	(283)	(283)
2009/10	7,838	(275)	(558)
2010/11	7,753	(85)	(643)
2011/12	7,361	(392)	(1,035)
2012/13	7,314	(47)	(1,082)
2013/14	7,329	15	(1,067)
2014/15	7,255	(74)	(1,141)
2015/16	6,994	(261)	(1,402)

This budgeting change regarding vacant positions and corresponding vacancy savings has caused some confusion in developing this year's budget, particularly from those departments that rely heavily on this budgeting strategy to support other unbudgeted projects and programs. This confusion has caused some departments to submit a supplemental budget request, even though they had budgeted much more in vacancy savings in this fiscal year than the actual supplemental budget request. For example, the Superior Court budgeted $2,108,807 in vacancy savings for this year's budget but submitted a supplemental request for FY 2015/16 of $1,500,545. The Juvenile Court budget submitted a vacancy savings of $2,338,277 for this year but submitted a supplemental funding request of $1,494,014 for next year. The Sheriff budgeted $8,200,000 in vacancy savings for this fiscal year and $1,800,000 for next fiscal year.

We will work with all County departments that relied excessively on budgeting vacant positions and offsetting it with some form of vacancy savings to ensure their budget expenditures are reflective of the actual projects and programs of the department or agency, which significantly increases budget transparency and accountability.

V. RECOMMENDED ADJUSTMENTS TO GENERAL FUND BASE EXPENDITURES

As discussed in prior sections above, the projected base revenues of $542,550,218 are only $633,462 less than are required to fund projected base expenditures of $543,183,680. If no further changes to expenditures were required, the General Fund's budget could be balanced with minimal adjustments. Unfortunately, additional outside events occurred, which threw the budget significantly out of balance.

As part of balancing their budget, the State accelerated cost transfers to the counties and increased cost transfers to Pima County by more than any other county in the state. The proposed cost transfers to Pima County that are presently enacted into law range from $12.8 million to $23.2 million. The fact that the final amount of cost transfers will not be determined by the State Property Tax Oversight Commission until sometime in September 2015, long after we have adopted a budget and set a tax rate on the dates required by law, requires the budget to account for the worst-case scenario of State budget cost shifts.

Table 4 below details the expenditure adjustments required to assume the additional State-related costs, fully fund a 6 percent budget reserve and other recommended adjustments to the FY 2015/16 base expenditures and operating transfers-out.

Table 4: Recommended Adjustments to FY 2015/16 Base Expenditures and Operating Transfers-Out.

Proposed FY 2015/16 Expenditures and Operating Transfers-Out	**$543,183,680**
Uses of FY 2014/15 Ending Fund Balance:	
Banner-University Medical Center South Campus	$12,500,000
Fund Portion of 6 Percent Budget Reserve	$19,347,551
State Budget Cost Shifts:	
Homeowner Tax Rebates (1Percent) – Minimum Payment to School Districts	$8,051,797
State Juvenile Corrections	$1,840,289
Restoration of ALTCS Dental	$141,000
Arizona Department of Revenue Costs	$1,541,775
2 Percent Reduction in General Fund Departmental Expenditures	($6,970,364)
Reduce Pavement Preservation Program	($5,000,000)
Juvenile Court-Absorb Juvenile Corrections Cost Shift	($1,840,289)
Stadium District-One-Time Reduction of General fund Support	($1,000,000)
Clerk of Superior Court-Unfund Collections Unit	($553,101)
Parks-Move Additional River Parks Maintenance Costs to Regional Flood Control District	($298,462)
10 Percent Reduction in Outside Agency Funding	($234,936)
Fund Remainder of 6 Percent Budget Reserve and Other Adjustments	$13,873,730
FY 2015/16 County Administrator Recommended Expenditures and Operating Transfers-Out	**$584,582,670**

Note: State Budget Cost Shifts do not include $1,249,116 reduction in Presidential Preference Primary Election Reimbursement.

Table 4 above contains an overstated Arizona Department of Revenue cost transfer of approximately $500,000. This will be adjusted at the time of Tentative Budget Adoption.

As can be seen, these adjustments include several negative amounts as funded programs are cancelled within the budget to fund a major portion of State budget cost shifts. The uncertainty regarding the amount of County funds required to cover the cost shifts, varying from $12.8 million to $23.2 million, amplifies the need for a larger budget reserve. The program reductions to meet the State cost transfers include across-the-board (two percent) budget reductions and targeted budget reductions. These target budget reductions from the General Fund will have serious service impacts; in particular, the $5 million the Board has, for the last several years, allocated to pavement preservation due to the lack of adequate State funding for transportation. This allocation is in jeopardy due to the excessive cost transfers that have impacted Pima County this year more than any other county, including

Maricopa, which has a four times larger population. Other serious budget impacts will occur in the area of juvenile detention.

Without a doubt, these reductions will have an impact on the level of services that are provided by County departments for various programs.

The General Fund budget I recommend totals $584,492,670 and consists of $551,689,798 of expenditures and $32,802,902 of operating transfers-out to other County departments.

I am also recommending a General Fund Budget reserve of $32,849,201. This amount represents 6 percent of recommended revenues and operating transfers-in. This reserve not only meets the Government Finance Officers Association recommendation of a minimum set aside but will also accommodate the possibility that the County will be required by the State to pay the worst-case cost of the payment to school districts for qualifying properties that fall under the homeowner one-percent cap on primary property taxes as discussed above and still retain a reserve capacity for any emergency funding during the course of the coming fiscal year. A further discussion of the value of this reserve occurs in Section III.B.2.

VI. RECOMMENDED ADJUSTMENT TO GENERAL FUND BASE REVENUES

The adjustments to expenditures and operating transfers-out discussed in Section V above, despite all the reductions in funding for County services and programs, creates an imbalance between the base revenues and operating transfers-in plus the FY 2015 ending fund balance and the recommended expenditures and operating transfers-out of $10,094,901. Table 5 below shows the revenue adjustments required between the base revenues and operating transfers-in and the County Administrator recommended revenues and operating transfers-in.

Table 5: Recommended Adjustments to FY 2015/16 Base Revenues and Operating Transfers-In.

Proposed FY 2015/16 Revenues and Operating Transfers-In	**$542,550,218**
FY 2014/15 Ending Fund Balance	$31,847,551
Increase Primary Property Tax Rate by $0.1098 to offset $8,051,797 of State Cost Transfers	$8,054,241
State Budget Cost Shifts:	
Reduction in State Reimbursement for Presidential Preference Primary Election	($1,249,115)
Reimbursement from Regional Transit Authority for Arizona Department of Revenue State Transfer	$1,514,775
County Attorney Transfer Portion of Employer Sanctions Cash Balance to the General Fund	$1,000,000
Sheriff Increase in Correctional Housing Reimbursement	$700,000
Forensic Science Center Proposed Fee Increase	$75,000
FY 2015/16 County Administrator Recommended Revenues and Operating Transfers-In	**$584,492,670**

Please note that the State is still processing each jurisdiction's share of the costs of funding the Arizona Department of Revenue. It is likely this revenue amount will be significantly reduced in the Proposed Tentative Adopted Budget.

In prior election cycles, the State has reimbursed Pima County for the costs of holding the State's Presidential Preference Primary Election. This reimbursement was reduced from 100 percent to $1.25 per active voter. The State Legislature did not even appropriate sufficient funds to fully cover even this lower amount in the State Budget. The original base County revenues were developed using the full reimbursement model that had been promised by the Legislature, and the Recommended Budget has been reduced in expectation of the decreased reimbursement.

The State Legislature apparently believes it is appropriate that counties begin to share in the administrative expense of collecting and distributing sales tax revenue in Arizona. This is particularly unreasonable, as we do not levy a sales tax. The Arizona Department of Revenue does collect a countywide sales tax on behalf of the Regional Transportation Authority.

As part of the process of identifying reduced costs and other revenue sources to offset the State budget cost shifts' impacts to the County, additional revenue sources were identified. The County Attorney will appropriately be transferring $1 million of funding from the State as part of the Arizona Employers Sanction Law. The Sheriff's Office has identified $700,000 in additional correctional housing fees that will be billed to the State. The Forensic Science Center will update their fee schedule for services provided to client jurisdictions.

As discussed above, costs have increased for a variety of reasons. These include increases in mandated payments such as retirement contributions, increased employee costs for insurance, increased costs of obtaining services, increased costs incurred during an election year and increased costs required to maintain adequate central services infrastructure. The accelerated State budget cost shifts of between $12.8 million and $23.2 million have exacerbated County costs and the uncertainty of the real impact of these cost shifts to the point where, the County, despite our best efforts, is unable to absorb the full impact of these new costs.

We expect the County will, at a minimum, need $8,051,797 to provide the "additional state aid for education" to school districts in which the constitutional cap on residential property taxes is exceeded, which was previously provided by the State. (The legislation is so unclear, and so much of the allocation is left to the Property Tax Oversight Commission, that it is impossible to determine at this point the exact extent of the County's liability. Most or all of this will go to Tucson Unified School District (TUSD), which is required by

State law to raise all of the funding for its federally-mandated desegregation program from local property taxes and, consequently, has a higher tax rate than would otherwise be required. I am, therefore, recommending the Board approve an increase in the County's FY 2015/16 primary property tax rate from $4.2779 to $4.3877, a $0.1098 increase. We will be levying this tax essentially for the general support of TUSD as required by the State.

As you know, the County Attorney has been authorized to file a lawsuit to reverse what we believe is an unlawful transfer of State responsibility for school funding. The one percent of full cash value cap on total property taxes for residential property was created by a 1980 Constitutional Amendment. One year later, in 1981, the Arizona Legislature implemented the cap by absorbing overages as part of its constitutional obligation to provide for a uniform statewide school system. After paying this cost for the last 34 years, the Legislature, this year, shifted the cost to local jurisdictions. We anticipate that the Property Tax Oversight Commission, which has been given the discretion to determine how much each jurisdiction will pay, will allocate most of the responsibility for the TUSD payment to the County. If a final court decision striking down this new legislation is rendered before the statutory date of tax levy and rate adoption, which is August 17, 2015, I will recommend the Board reverse the rate increase. If a final Court decision striking down the legislation is rendered after that date, I will recommend the Board rebate this tax increase when the budget for FY 2016/17 is adopted. The sole reason our property tax rate will increase this year is State budget cost transfers. We have absorbed all of these transfers, but we cannot absorb the "additional state aid for education" portion.

I have made it clear throughout this memorandum that the State has placed Pima County in an extremely difficult position by, in some cases, arbitrarily shifting its costs to the County. In a year of improving taxable net assessed values, the State has placed the County in a position where, despite reducing costs and increasing other revenues, we must raise our primary property tax rate. It is important the taxpayers are made aware of this shift in tax burden. In order to make this clear to County property taxpayers, I will be including a notice with the property tax bills sent to each individual taxpayer that explains that as much as $106 million, or 33 percent, of the primary property tax they pay goes for programs the State has mandated County taxpayers fund rather than the State.

Below is a draft of the notice of State cost transfers and the required County property tax increase:

NOTICE OF STATE COST TRANSFERS REQUIRING A COUNTY PROPERTY TAX INCREASE

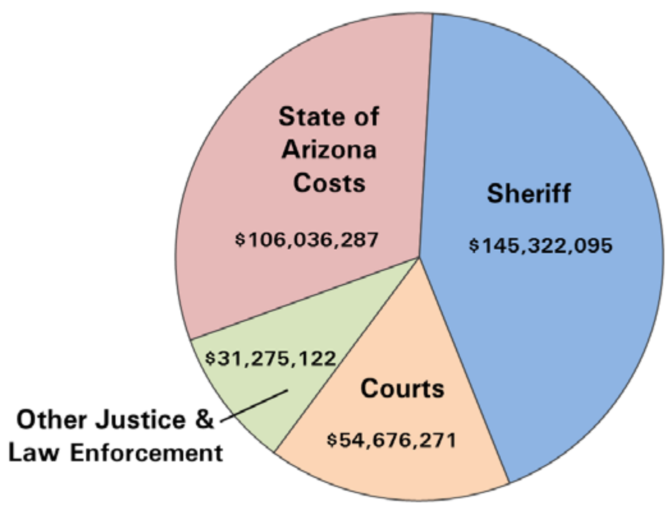
Approximately one third, or 33 percent, of your County primary property tax is transferred to the State of Arizona, or to other entities on behalf of the State, to support the State budget. Last year, $82.8 million was sent to the State. This year, the State will require up to $106 million in local taxpayer support. This is an increase of $23.2 million; 28 percent in a single year. The bulk of those funds are being used to pay for a program the State has funded for the last 34 years.

The County has absorbed most of this cost by reducing the County budget approximately 2 percent.

Unfortunately, we were unable to absorb all of this State cost transfer and are required to increase our property tax levy by $8.1 million, or 2.5 percent, to help cover all of the State cost shifts. The County believes up to $18.6 million of this cost shift is unlawful and will ask the Courts to rule invalid the State legislation requiring this cost shift. If a Court timely rules the transfer unlawful, this will enable the County to rebate the $8.1 million property tax increase back to taxpayers by lowering our property tax levy next year by an equal amount.

The chart below shows where your County primary property tax is spent.

HOW YOUR $337.3 MILLION PIMA COUNTY PRIMARY PROPERTY TAX IS SPENT



Note: FY 2015/16 Recommended Pima County Primary Property Tax Revenue Is $337,309,775.

Note: The expenditures of the Justice and Law Enforcement function as a whole are greater than the total included in the chart above. The remaining expenditures are offset by other General Government and departmental revenues.

As you can see, a large portion of your County primary property tax is sent to the State for its use.

VII. THE OVERALL BUDGET

A. Special Districts and Debt Service

1. County Library District

The Library District is funded by a dedicated secondary property tax and serves the entire County. In FY 2015/16, the Pima County Public Library budget includes the operation of a Main Library; 22 branches; a bookmobile; and online services, including a dynamic web portal, Infoline, Ask a Librarian, online homework help, employment and career help, full-text magazine and journal articles and downloadable e-books, audiobooks, video and music.

The Library provides numerous community services, including online and in-person homework tutoring for students of all ages, tax preparation assistance, computer instruction, and special assistance for small businesses, nonprofit organizations, entrepreneurs, job seekers and the unemployed. The Library has a collection of 1.3 million catalogued items, which will be borrowed over 5 million times in the course of a year. The Library provides nearly 1,000 computers that generate 3 million computer sessions by the public, welcomes 6 million visitors through its doors each year, and nearly half of all Pima County residents hold Pima County Public Library cards. The Library offers an increasing number of digital items to its patrons, including e-books and downloadable audiobooks as well as streaming video. Community groups use library meeting facilities to hold meetings of civic and educational interest, and these facilities are gathering places where people interact, share information and engage in creating content through 21st Century Skills.

Partnerships initiated by the Library provide educational opportunities, contribute to economic development and increase the quality of life for everyone in Pima County. Partners such as Pima Community College Adult Education, Literacy Connects and Make Way for Books allow for increased literacy services such as GED preparation and English Language Acquisition classes. Collaboration with the Metropolitan Education Commission allows the Library to provide information about financial aid and career exploration to high school students. The Library also partners with Pima County OneStop, the Arizona State Library Archives and Public Records, and the Arizona Department of Economic Security to provide job help classes and skills training for the unemployed. The Library is also a founding partner and steering committee member of the Tucson Festival of Books.

Since 2012, the Pima County Public Library has partnered with the Pima County Health Department to place public health nurses in libraries. This unique and award-winning intervention serves patrons with significant social and behavioral health challenges, ensures that public health services are readily available, and creates safer and more welcoming environments for customers. Currently, there are 18 public health nurses at 20 branch libraries, including five who are trained as Arizona Department of Economic Security Application Assisters. The Library Nurse project has been recognized in *Library Journal Online* and *Public Libraries* Magazine, as well as *Nurse.com* Magazine.

The County Library District's secondary property tax base is increasing for the first time since 2010. The District's Secondary Taxable Net Assessed Value declined 3.9 percent in FY 2013, 6.47 percent in FY 2014, and 0.89 percent in FY 2015. In FY 2015/16 the tax base will increase a modest 1.3 percent.

The FY 2015/16 Recommended Budget for operating costs, grants and operating transfers-out is $40,258,747, which is a $1,425,302 increase from the FY 2015 budgeted amount of $38,833,445. The recommended budget will fund increased operating expenses for books and materials, information technology, facilities management, finance and other internal service charges and maintenance costs.

To achieve structural balance in the Library District budget, the tax rate will need to be increased by $0.06 and operating expenses reduced by $1.5 million to retain an approximate 10 percent fund balance. Approximately $200,000 per year in operating expenses can be reduced by closing eight libraries on Sunday when use is minimal. It has also been proposed that the Dewhirst-Catalina, Dusenberry-River, Geasa-Marana and Santa Rosa Libraries be closed. As an alternative to closing these four libraries, other cost savings measured could be introduced.

Some have portrayed the possible closing of these libraries as an indication we cannot support ongoing operating and maintenance expenses for the library system. In particular, how can we plan for new libraries when we cannot operate those we already have?

This is an incorrect assumption. Closing small, obsolete, particularly difficult to maintain, or located on our boundary is an action to maximize efficiency. The larger regional libraries serve more people at a lower cost.

Of the four libraries recommended for closure, one – the Geasa-Marana Branch – should be closed because of low use and a future renovation cost of nearly $700,000. The remaining three branches could remain open, but their hours of operation would be adjusted to reflect actual times of significant usage.

The least used day of the week for our libraries is Saturday. When libraries have offered story times and other programming on Saturday, attendance has consistently been low; the same is true for workshops, computer classes and other events. Families have many Saturday commitments. Closing Saturday and adjusting hours to coincide with use levels could save an additional $400,000 or more. We need to be as cost effective as possible in delivering library services and that means adjusting hours of operation based on utilization.

By adjusting hours of operation, delaying some remodeling and closing only one outdated, small library, it is possible to keep all remaining libraries open and remain within the $0.06 tax rate increase and a fund balance of between 5 and 10 percent.

Staff will continue to refine the Library budget for Board consideration; and by the time of Tentative Budge Adoption, we should know whether the rate increase should be adjusted upward by another $0.01.

The requested Library District property tax rate for FY 2015/16 is $0.4953 per $100 of taxable assessed value, which is an increase of $0.0600 over the FY 2015 rate of $0.4353. The increased property tax rate is necessary to fund the recommended budget because the Library District fund balance has been reduced substantially; and without this increase, the fund balance is projected to fall well below the recommended 10 percent of revenues to less than 2 percent. This is the result of a multiyear plan beginning in FY 2010 to reduce the Library District fund balance by deliberately under-budgeting tax revenue. This increase will stabilize the District's fund balance moving forward.

The recommended tax rate is projected to provide $37,261,314 in revenues that will be supplemented by a projected $2,340,000 from fines, interest, grants and miscellaneous revenue and $657,433 from the Library District fund balance in order to meet the recommended overall budget of $39,601,314. This recommended budget will reduce the ending fund balance from a projected ending fund balance of $3,204,877 at the end of FY 2014/15 to $2,547,444 at the end of FY 2015/16.

2. Debt Service Fund

The total Recommended FY 2015/16 Debt Service Fund budget is $110,820,702, a $4,133,120 decrease from the current fiscal year. The Debt Service Fund includes payments on the County's General Obligation debt, the Street and Highway Revenue Bond debt, and Certificates of Participation debt, all of which are long-term debt.

General Obligation Debt Service

The County's General Obligation Debt Service is funded with a secondary property tax levy. The recommended General Obligation debt service of $53,712,831, an increase of $588,181 from FY 2015, will fund existing debt service as well as debt service on a proposed $25,681,000 bond sale expected to occur in the spring of 2016.

As originally planned when the bond program began, debt service on new bond sales supported by the secondary tax levy is being offset by ongoing reductions in debt service for existing outstanding bonds. As old bonds are being retired, new bonds are being sold, incurring new debt. The amount of debt that can be supported is limited by a Board-imposed cap on the tax rate for debt service. This rate cap is 0.8150. The County manages the issuance of its debt to provide funding as needed to maintain the ongoing capital improvement program. The County generally issues debt on an annual basis for General

Obligation bonds to time the issuance of debt to minimize the outstanding balances and manage the level of debt service to avoid significant spikes in payments in any given year.

The County has several major capital improvement projects next fiscal year, including the completion of the Public Service Center and Fleet Service's Fuel Island at Mission Road; design for the new Pima Animal Care Center; flood control, erosion control, and urban drainage; and various park improvement projects.

I recommend the General Obligation Debt Service tax rate remain unchanged at $0.700 per $100 of assessed value for FY 2015/16.

Street and Highway Revenue Debt Service

The 1997 Transportation Bond authorization provides for the sale of Street and Highway Revenue bonds with the debt service being repaid from the Highway User Revenue Fund (HURF) monies our Department of Transportation receives from the State. The recommended Street and Highway Revenue bond debt service of $18,563,708, a decrease of $320,061 from FY 2015, will fund existing debt service.

Certificates of Participation Debt Service

The Certificates of Participation debt service of $38,544,163, a decrease of $4,401,240 from FY 2015, includes the Certificates of Participation issued in prior years for the acquisition or construction of County facilities such as the Public Service Center, the Bank of America Building, the Fleet Services Facility, and various sewer projects. Certificates of Participation debt service is paid from funds other than the General Obligation debt service tax levy.

Sewer Debt Service

In addition to the debt service included in the Debt Service Fund, Pima County has debt service that is included in the Regional Wastewater Reclamation Enterprise Fund and paid for with sewer system revenues. Of the County's $1.3 billion debt, $137,650,000 is for sewer revenue bonds, $494,130,000 is for sewer revenue obligations, and $19,679,697 is for loans from the Water Infrastructure Finance Authority of Arizona (WIFA); this total of $651,459,697, or 49 percent, is the direct debt of the County and is repaid solely from sewer system revenues with no impact on the overall Debt Service Tax Rate. In addition to the direct sewer debt, another $24.7 million of the remaining County debt consists of Certificates of Participation issued to pay for sewer projects. In total, debt for sewer infrastructure is approximately 51 percent of all County debt.

3. Regional Flood Control District

For the first time in six years, the value of the Regional Flood Control District's (RFCD's) secondary property tax base is forecasted to increase. The RFCD's secondary net assessed value declined 4 percent in FY 2011, 10.5 percent in FY 2012, 5.1 percent in FY 2013, 6.57 percent in FY 2014 and 0.02 percent in FY 2015. The RFCD's tax base is forecasted to increase by 2.21 percent in FY 2015/16. The RFCD has responded to past declines by closely monitoring and controlling costs and by reducing the amount of funding transferred to its Capital Improvement Program in order to maintain a consistent property tax rate.

The recommended operating budget for the various components of the RFCD is $17,490,112, which is $393,384 more than the current year budget, and reflects increased costs of operations, engineering services, and repairs and maintenance to new and existing flood control facilities. This amount also includes $368,370 of grant-related expenditures.

The overall RFCD Fund's recommended budget also includes $1,000,000 of revenue and $967,900 of expenditures related to a future Canoa Ranch In-Lieu Special Revenue Fund. This fund is used to design, construct and maintain ecosystem restoration within the Canoa Ranch In-Lieu Fund project site.

Also recommended are operating transfers-out of $6,725,504 including $6,405,941 to the Capital Projects Fund, $189,602 to the Stadium District for operating and maintenance costs of the Kino Environmental Restoration Project, $20,000 in funding for the County's Native Plants Nursery, $46,370 of Flood Control Grants match and $63,591 to the Debt Service Fund for the RFCD's share of debt service on Certificates of Participation issued in 2010 for the Countywide Enterprise Accounting System. This represents a decrease of $3,698,220 in operating transfers-out from the current fiscal year.

Flood Control Capital Projects funds are used to acquire, construct, expand and improve flood control facilities within the County, including bank stabilization, channels, drainage ways, dikes, levees, and other flood control improvements. This includes funding to provide federal- and state-mandated floodplain management services and to continue the Board-approved Riparian Protection Program as a component of the Sonoran Desert Conservation Plan and to procure floodprone land contiguous to existing watersheds within the County. These land acquisitions serve the dual purpose of protecting existing riparian habitat corridors and preventing future flood damages.

This year, an additional $298,642 in General Fund expenses from the Natural Resources, Parks and Recreation Department (NRPR) are being transferred to the RFCD for maintenance of the regional river park system. The annual operating and maintenance expenses for the system will be fully funded by RFCD.

River parks are a regulatory outgrowth of permitting river channelization and bank stabilization. They are required as a condition of a federal Clean Water Act Section 404

Dredge and Fill Permit issued by the US Army Corp of Engineers. Today, the river parks are the County's largest and most used recreational facility. They are operated solely by RFCD through funding agreements with NRPR. It is likely few residents fully understand the County's responsibility in funding of the river park system through the RFCD secondary property tax. This year, efforts will be made to educate taxpayers about these benefits.

I recommend the RFCD's FY 2015/16 tax rate be increased $0.0100 to $0.3135 per $100 of assessed value in order to meet its existing and growing obligations by providing necessary adjustments to increased operational costs that have been deferred during the past six years of the economic recession and resulting contraction of the RFCD's tax base.

B. Annual Capital Projects Fund Budget and Capital Improvement Plan Budget

As shown in Table 6 below, the FY 2015/16 recommended Capital Improvement Plan of $133,968,553 consists of the Capital Projects Fund Budget of $81,349,477 and the Capital Projects of Regional Wastewater Reclamation of $47,507,510, Fleet Services of $2,186,827, Facilities Management-Garages of $735,000 and Telecommunications of $2,189,739. A complete list of projects for the Recommended Capital Improvement Plan is included in the Capital Projects section of this Recommended Budget Book.

Table 6: Recommended FY 2015/16 Capital Projects Fund Budget and Capital Improvement Plan Budget.

Capital Improvement Plan	FY 2015 Bond and Non-bond Project Budgets	FY 2015/16 Bond and Non-bond Project Budgets	Difference	1997 Bonds	2004/2006/ 2014 Bonds	Non-bonds
Capital Projects Fund						
Transportation	$ 62,056,308	$41,892,895	($20,163,413)	$3,230,818	-	$ 38,662,077
Facilities Management	33,915,787	14,070,808	(19,844,979)	-	$ 2,988,962	11,081,846
Sheriff's Department	4,561,707	-	(4,561,707)	-	-	-
Regional Flood Control District	15,138,247	11,994,819	(3,143,428)	24,841	1,588,220	10,381,758
Parks and Recreation	8,867,599	4,518,288	(4,349,311)	384,331	3,258,908	875,049
Open Space	6,304,623	1,963,228	(4,341,395)	-	1,963,228	-
Information Technology	4,194,935	337,126	(3,857,809)	-	-	337,126
Community Development	2,621,164	1,828,301	(792,863)	690,762	1,137,539	-
Environmental Quality	350,000	3,400,000	3,050,000	3,400,000	-	-
Elections	750,000	-	(750,000)	-	-	-
Office of Sustainability and Conservation	905,110	1,344,012	438,902	-	1,344,012	-
Total Capital Projects Fund	**$139,665,480**	**$ 81,349,477**	**($58,316,003)**	**$7,730,752**	**$12,280,869**	**$ 61,337,856**
Wastewater Reclamation Budget	$ 84,392,158	$ 47,507,510	($36,884,648)	-	-	$ 47,507,510
Fleet Services Budget	6,823,967	2,186,827	(4,637,140)	-	-	2,186,827
Facilities – Garages	-	735,000	735,000	-	-	735,000
Telecommunications Budget	1,551,878	2,189,739	637,861	-	-	2,189,739
Total Capital Improvement Plan	**$232,433,483**	**$133,968,553**	**($98,464,930)**	**$7,730,752**	**$12,280,869**	**$113,956,932**

Note: The total for the Capital Projects Fund excludes $11,065 of consulting expenses for arbitrage calculations.

1. Capital Projects Fund Budget

The recommended $81,360,542 Capital Projects Fund Budget for FY 2015/16 is a decrease of $58,304,938, or 42 percent, from the current year's budget of $139,665,480.

Of the total Capital Projects Fund, $7,730,752 is funded through 1997 bonds, $12,280,869 is funded through 2004/2006/2014 bonds, and the remaining $61,337,856 is funded through other non-bond sources including Regional Transportation Authority (RTA) sales taxes, impact fees, grants, Certificates of Participation and General Funds.

The Department of Transportation has budgeted $42 million for 36 projects. The projects include the Valencia Road: Mark Road to Wade Road for $8.8 million and the Hughes Access Road Relocation for $5.9 million. Funding for the FY 2015/16 Department of Transportation Capital Program consists of $10.7 million in RTA funding, $11.5 million in grants, $3.2 million in HURF bonds, $6.9 million in State revenue, $6.2 million in impact fees, and $3.4 million from various other funding sources.

Facilities Management has budgeted $14.1 million, which is a 59 percent reduction from the current year's budget. This year's requested budget includes $2 million for the new Animal Care Center funded with General Obligation bonds authorized by the voters in 2014. Three million dollars is budgeted for additional buildout of the Pima County Public Service Center funded with Certificates of Participation.

NRPR has budgeted $4.5 million for 10 projects, including Northside Community Park (Rillito) for $2.7 million funded with 2004 General Obligation bonds.

2. Regional Wastewater Reclamation Capital Budget

The FY 2015/16 recommended capital budget for the Regional Wastewater Reclamation Department (RWRD) is $47,507,510, a decrease of $36,884,648 from FY 2015. The FY 2015/16 Capital Program is planned to be funded entirely with RWRD obligations. Conveyance projects total $35.3 million, including $10 million for minor rehabilitation projects and $9.4 million for the North Rillito Interceptor Rehabilitation Project. Treatment projects total $11.5 million and include the Continental Ranch Regional Pump Station Modification project budgeted for $2.3 million and $1.8 million for sewer treatment improvements in Green Valley.

3. Fleet Services Capital Budget

The FY 2015/16 recommended capital budget for Fleet Services is $2,186,827, a decrease of $4,637,140 from FY 2015. The recommended budget includes $1.8 million for the Mission Road Complex Fuel Island that will be funded through Certificates of Participation.

VIII. COMBINED TOTAL COUNTY BUDGET

A. Combined County Property Tax Rate and Levy

The combined primary and secondary property taxes levied by the County fund 38.5 percent of the total County Recommended Budget expenditures. These are the only County revenues over which the Board has substantial control. The remainder of the County budget is supported almost entirely by charges for services and intergovernmental revenues, primarily State revenue sharing and grants.

As discussed in Section VII above, it is recommended that the County's primary property tax rate, which supports the County's General Fund, be increased by $0.1098 to $4.3877 per $100 of taxable assessed value. Pursuant to State Truth in Taxation Statutes, the levy produced by this tax rate will be over the neutral levy; and a Truth in Taxation hearing will be required to be noticed and held at the same time as Final Budget Adoption. The County's neutral levy is $4.3025 per $100 of taxable assessed value.

The County controls three secondary property tax rates and their associated levies: Library District, Regional Flood Control District and Debt Service. The Library District tax rate will increase by $0.0600 from the FY 2015 rate to $0.4953 per $100 of taxable assessed value. The property tax rate for the Regional Flood Control District will increase by $0.0100 from FY 2015 rate to $0.3135 per $100 of taxable assessed value. The property tax rate for Debt Service will remain unchanged from the FY 2015 rate of $0.7000 per $100 of taxable assessed value. The net of these changes in the secondary property tax rates will produce $5.5 million of additional revenue in FY 2015/16.

The result of these recommendations is a combined County property tax rate of $5.8965 per $100 of taxable assessed value, a $0.1798 increase over the FY 2015 tax rates. The FY 2015/16 recommended primary and secondary County tax rates are summarized in Table 7 below.

Table 7: Combined Recommended County Property Tax Rate.

Description	FY 2015 Adopted Rates	FY 2015/16 Recommended Rates	Difference
Primary	$4.2779	$4.3877	$0.1098
Library District	0.4353	0.4953	0.0600
Debt Service	0.7000	0.7000	0.0000
Regional Flood Control District	0.3035	0.3135	0.0100
TOTAL	**$5.7167**	**$5.8965**	**$0.1798**

For the first time in six years, the value of the County's overall property tax base will increase slightly next fiscal year. Consequently, the rates recommended above will be applied to a primary tax base that is 1.36 percent more than the current year's base and to secondary tax bases that range from an increase of 0.53 percent (Debt Service) to an increase of 2.21 percent (Regional Flood Control District). This net increase in the tax base, combined with the net changes in the primary and secondary property tax rates, results in the recommended combined County property tax levy increasing by $19,151,357, or 4.5 percent, more than the current year levy as shown in Table 8 below.

Table 8: Combined Recommended County Property Tax Levy.

Description	FY 2015 Adopted Levies	FY 2015/16 Recommended Levies	Difference
Primary	$321,633,141	$334,358,574	$12,725,433
Library District	32,747,156	37,743,651	4,996,495
Debt Service	53,059,292	53,342,531	283,239
Regional Flood Control District	20,539,235	21,685,425	1,146,190
TOTAL	**$427,978,824**	**$447,130,181**	**$19,151,357**

B. Combined County Budget

The combined Recommended County Budget, reflected in the budget schedules and departmental budget summaries following this memorandum, is $1,164,953,662. This is a $23,510,590, or a 1.98 percent, decrease from the FY 2015 Adopted Budget of $1,188,464,252.

IX. COUNTY PROPERTY TAX REDUCTION OPTIONS

In the past, the County's primary property tax rate of $4.27 per $100 of assessed value has been criticized as high. It is the highest of any county in Arizona. The average FY 2014/15primary property tax rate for a county in Arizona is $2.1788. One of the primary reasons our tax rate is the highest is that Pima County is the only county in Arizona that does not have a separate, dedicated excise tax for supporting County operational expenses.

Table 9 below shows the various county excise taxes available and used in other counties to offset their reliance on property tax for County operational expenses.

Table 9: Fiscal Year 2014/15 County Property and Sales Tax Rates.

County	Primary Property Tax Rate	County General Fund Excise Tax	Public Health	Jail Excise Tax	County Road Tax	Healthcare District	County Capital Projects
Apache	$0.4810	0.50%	$0.1260	$0.2916 SPT	—	—	—
Cochise	2.6276	0.50%	—	—	—	—	—
Coconino	0.5646	0.50%	$0.2500	0.50%	0.30%[1]	—	—
Gila	4.1900	0.50%	—	0.50%[2]	—	—	—
Graham	2.1794	0.50%	—	0.50%[3]	—	—	—
Greenlee	0.5500	0.50%	$0.2300	—	—	—	—
La Paz	2.2863	0.50%	—	0.50%	—	—	—
Maricopa	1.3209	—	—	0.20%	—	$0.1856	—
Mohave	1.8196	0.25%	—	—	—	—	—
Navajo	0.8185	0.50%	$0.2430	—	—	—	—
Pima	4.2779	—	—	—	—	—	—
Pinal	3.7999	0.50%	0.10% ET	—	0.50%	—	—
Santa Cruz	3.6471	0.50%	—	0.50%	—	—	—
Yavapai	1.9580	0.50%	—	0.25%	—	—	—
Yuma	2.1608	0.50%	0.112% ET	0.50%	—	—	—

SPT = Secondary Property Tax, listed as a dollar tax rate

ET = Excise Tax, listed as a percentage

[1]Coconino County road tax effective January 1, 2015

[2]Gila County voters approved a half-cent jail excise tax effective July 1, 2015

[3]Graham County voters approved a half-cent jail excise tax effective July 1, 2015

Source: County Supervisors Association of Arizona

Several options exist for reducing the County's primary property tax rate. These options are as follows:

A. Reverse State cost transfers

As discussed previously in this memorandum, our primary property tax rate is used to support State programs. For FY 2015/16, this amount is expected to increase to nearly $106 million, or one third of our primary property tax rate. If the State were to pay for their programs using State funds, our primary property tax rate could be reduced from $4.3877 to $2.9422.

B. Adopt a half-cent sales or excise tax

Pima County has the option to adopt a half-cent sales tax by unanimous vote of the Board. If such a tax were enacted and used to reduce our property tax, our property tax rate would decrease another $0.9539, from $2.9422 to $1.9883.

C. Adopt a jail excise tax

The County has the authority to levy a quarter-cent jail excise tax upon approval at a General Election by the voters of Pima County. If approved, a jail excise tax would further reduce the County property tax rate by $0.4769, from $1.9883 to $1.5114.

As can be seen, if these three strategies were fully utilized, the County's primary property tax rate would decrease from $4.3877 to $1.5114. It would then be $0.6674, or 31 percent, below the statewide average.

If the Board wishes to reduce property taxes, it will need to authorize one or more excise or sales taxes.

CHH/mjk

Attachments