

COUNTY OF MILWAUKEE
Inter-Office Communication

Date: May 17, 2023

To: Marcelia Nicholson, Chair, Milwaukee County Board of Supervisors

From: Joe Lamers, Director, Office of Strategy, Budget and Performance

Subject: 2024 Operating Budget Gap and Budget Process Updates

File Type: Informational Report

OVERVIEW

This report provides a preliminary operating budget gap estimate for 2024, as well as updates pertaining to the annual budget process.

The Office of Strategy, Budget, and Performance (SBP) at this stage projects a budget gap of \$21.0 million for Fiscal Year 2024. This gap is part of an ongoing structural deficit, whereby growth in revenue is not sufficient to keep pace with inflationary operating cost growth. In addition to the ongoing imbalance between revenue and expenditure growth, major cost drivers for the 2024 budget include an increased pension contribution (largely due to investment performance in 2022) and investments in compensation.

BACKGROUND

Milwaukee County has been operating with a structural deficit dating back to the early 2000's. County officials and policymakers have repeatedly been required to focus budget planning efforts on where to reduce expenditures while opportunities to raise revenue and make new investments are limited. The ongoing imbalance is caused by stagnant revenue growth which is limited by State statutes and is not sufficient to keep pace with inflationary operating cost growth, or with increases in legacy healthcare and pension expenses. Between 2012 and 2023, policy makers have been required to close cumulative budget gaps of approximately \$350 million or an average of roughly \$30 million per year. While the budget has been balanced as legally required on an annual basis, the structural deficit persists and is projected to continue. The most recent five-year financial forecast prepared by the Comptroller's Office projected a cumulative operating budget gap of \$110 million by 2028.

FIVE-YEAR FORECAST COMPARISON

The 2024 budget gap estimate of \$21.0 million provided in this report is comparable but higher than the 2024 structural deficit estimate included in the Comptroller's Five-Year Fiscal Forecast that was presented to the County Board in March 2023 (File 23-411). The Five-Year forecast projected a gap of \$18.2 million for 2024. The increased gap estimate included in this report is primarily related to updates pertaining to projections and assumptions on compensation, vacancies and turnover rates.

SBP will continue to monitor the gap and will provide updates to the County Board when there are significant changes to budget estimates.

ANALYSIS

Based on preliminary estimates, the County will be facing a 2024 operating budget gap of \$21.0 million. Major factors contributing to the budget gap are shown in the chart below. These amounts reflect projected increases in expenditure items compared to 2023, removal of one-time revenue sources included in the 2023 budget, and increased revenue projections, which are shown in the chart as negative values because they reduce the projected gap amount.

2024 Operating Budget Gap Estimate	
Description	Amount
Compensation	\$ 6.9
Health Care	\$ 9.0
Pension	\$ 4.8
Debt Service P&I	\$ 1.0
Transit	\$ 10.4
Other Operating Cost to Continue	\$ 10.0
Total Expenditure Change	\$ 42.1
Revenue Change - Lost Revenues	
Debt Service Reserve	\$ 7.8
Unclaimed Revenue	\$ 1.3
Corrections ARPA to Levy	\$ 1.3
Revenue Change - Increased Revenue	
Property Tax	\$ (3.1)
Property Tax - DS	\$ (1.0)
Sales Tax	\$ (6.8)
Transit Revenue	\$ (9.1)
Investment Revenue	\$ (6.4)
VRF	\$ (0.3)
Other / Reimbursement Revenue	\$ (4.8)
Total Revenue Change	\$ (21.1)
Gap Total	\$ 21.0

The following descriptions provide additional information regarding assumptions used to develop the estimated gap. The numbers presented here are based on estimated changes from the 2023 budget and are subject to variability as the budget process continues.

Expenditures:

Compensation Increases: The 2024 budget gap estimate assumes \$6.9 million in new costs related to compensation increases. This includes \$1.4 million to annualize the

2023 Q2 general increase, \$2.7 million for a projected 2024 Q2 2% general increase, \$1.8 million to annualize the 2023 budget central salary adjustment (assumed to be implemented mid-year 2023), and \$1.0 million in new central salary adjustment funding for 2024.

Health Care: The Office of the Comptroller (in the 5-year forecast File #23-411) projects medical claims to increase roughly 4% and pharmacy claims to increase roughly 9%. There is uncertainty in the 2024 health care costs based on the number of positions that are filled.

Pension: Preliminary data from the County's pension actuary shows that the 2024 country contribution to the pension system will increase by \$4.8 million compared to 2023. The major factors for the cost increase are the normal cost increase, regular changes to actuarial assumptions approved by the Pension Board, and amortization of significant investment losses from the 2022 calendar year.

Debt Service P&I: An increase of \$1.0 million is a preliminary estimate of growth in debt service principal and interest costs. There is also a corresponding increase in property tax to coincide with the increase in debt service expenses, meaning that this increase is not expected to add to the overall budget gap.

Transit: The Office of the Comptroller (File 23-411) projects a 6.3% increase from the 2023 budget, which is roughly \$10.4 million.

Other Operating Cost to Continue: A \$10.0 million increase is estimated for inflationary operating costs excluding items already quantified in the above categories. This primarily relates to inflation on contracted commodities and services costs.

Revenues:

Debt Service Reserve: The 2023 budget included \$7.8 million in funding from the Debt Service Reserve which is considered a one-time revenue source. This report assumes that one-time revenue sources will not continue into 2024.

Unclaimed Revenue: Every other year, the County Treasurer advertises the possession of unclaimed funds. In 2024, no revenue is expected which is a decrease of \$1.3 million from the 2023 Budget.

ARPA to Levy – Corrections Pay: In recent years, the County approved using ARPA to pay for certain correction officer pay increases. The County's policy since then has been to phase out ARPA funding and phase in tax levy funding. The 2023 budget included \$2 million of ARPA for correction officer pay. The 2024 budget is expected to include \$1 million of ARPA for a tax levy increase of \$1 million. It is also expected that the 2025 budget will not include any ARPA for correction officer pay.

Property Tax: A total property tax increase of \$4.1 million is projected for the 2024

budget. This includes \$1.0 million of debt service levy that offsets the \$1.0 million of increase debt service expenditure and \$3.1 million of operating levy, reflecting the estimated maximum increase under state law.

Sales Tax: Based on strong recent economic activity, sales tax is projected to increase by \$6.8 million in the 2024 budget. Due to the volatility of sales tax activity and disbursements, this is a very preliminary estimate and will be monitored closely by SBP and the Office of the Comptroller.

Transit Revenue: Of the \$10.4 million projected increase in transit operating costs, \$9.1 million is projected to be offset by federal revenue. The availability of this federal revenue in 2025 is very uncertain and is a significant budgetary issue for the County to address.

Investment Revenue: The Office of the Comptroller (File 23-411) projects an increase of \$6.2 million in investment revenue. This is due to recovery from 2022 market losses and a high average daily balance due to federal stimulus funding and the debt service reserve.

Other/Reimbursement Revenue: \$4.8 million of other revenues are projected. This is primarily based on an estimate that approximately 15% of cost increases can be covered with outside reimbursement revenue, primarily for services in the airport and health and human services.

STATE BUDGET

SBP is monitoring several items including the State budget which may have a significant impact on the 2024 budget but are not currently included in the budget gap estimate.

The Governor's Proposed State Budget for 2023-2025 was released in February. The Proposed Budget is now under review by the state legislature. The Senate and Assembly are expected to act on the budget in June, and then the Governor is scheduled to sign the budget and issue vetoes in July.

The Proposed State budget includes several items which would impact the County's fiscal outlook for 2024 and future years. Significant provisions included in the Proposed Budget include but are not limited to the following:

- Allow for a 1% sales tax increase in Milwaukee County split between the City and County, and allow other counties and municipalities over 30,000 to impose an additional 0.5% sales tax
- Shared revenue reform: \$576 million statewide increase in shared revenue with future allocations tied to a formula that would grow with inflation
- Adjusting the tax levy limit to allow for 2% growth or net new construction
- 4% increase in transit, paratransit and general transportation revenues
- Revision to Youth Aids funding formula
- Other proposals that would impact County department revenues

These and other items will be monitored closely in the coming months.

CLOSING THE BUDGET GAP

Budget instructions were provided to departments in early April. These instructions included a tax levy target indicating that departments should be submitting requested budgets with a requested tax levy amount that is no greater than flat compared to the adopted 2023 budget. Adjustments to the levy target are made for compensation commitments. The flat levy target is estimated to provide approximately \$10 million of savings against the budget gap estimate, given that departments will need to absorb and self-fund inflationary cost-to-continue growth to stay within the target. The County will need to identify additional strategies during the budget process to reduce expenditures and/or increase revenue to balance the 2024 budget. Additional updates on options being considered will be provided during the budget process.

NEXT STEPS: 2024 Budget Process

Resolving the operating budget gap will be done through the budget process which takes place through the following timeline:

- Forecasting and Budget Strategy Phase:
 - January–April – SBP prepares forecasts for the upcoming fiscal year and develops budget assumptions with the County Executive and County Board
- Department Request Phase:
 - April – Departments receive operating budget instructions
 - April - July – Departments develop their budget requests
 - July – Departments submit their budget requests to SBO
- Recommended Budget Phase:
 - August-September – County Executive works with SBP and departments to finalize the Recommended Budget
 - October 1 – County Executive submits the Recommended Budget
- County Board Phase:
 - October-November – Finance and Audit Committee reviews and requests information on the Recommended Budget
 - November – The County Board adopts the budget

Throughout this process, SBP will provide additional information and updates.

ALIGNMENT TO STRATEGIC PLAN

3B: Enhance the County's fiscal health and sustainability

FISCAL EFFECT

The report is informational only and there is no fiscal impact.

VIRTUAL MEETING INVITES

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