
**THE SALT LAKE COUNTY AUDITOR'S
2006 BUDGET MESSAGE**

**Sean Thomas
Salt Lake County Auditor**

to the

Salt Lake County Council

**And To the Mayor and Citizens of Salt Lake
County**

December 6, 2005

Introduction

In accordance with the Uniform Fiscal Procedures Act for Counties (§17-36 of the Utah Code), the *Budget Officer* of the County is charged with preparing a Budget Message to explain the Council recommended budget, and in general, summarize significant changes in the County's financial position; revenues, expenditures, budgets, and additions or changes in policy.

I am pleased to have the opportunity as the Budget Officer of Salt Lake County, to present this Budget Message. My responsibility, acting in this capacity, and as an independently elected official, is to act as an advisor to the County Council and Mayor in financial and budget matters, and, as a guardian of the public trust as it relates to fiscal responsibility and accountability.

Every budget is a reaction to perception of current public needs. In certain cases, a new budget must also respond to prior significant decisions made to meet such public needs. Always, the budget must balance needs that can be met and those that must be deferred.

Economic Outlook

As the Budget Officer for the County, I am responsible for projecting revenues for the upcoming year. Our economy continues to show robust growth throughout 2005. Year-to-date sales tax revenues have increased substantially in comparison with the same period in 2004. Our 2006 revenue projections are included as a part of the Recommended Budget. These projections are based on our research, analysis of economic conditions, review of other governmental studies, consultation with others (in industry), and our revenue forecasting models.

To further refine and improve the County's revenue projection process, three years ago our office undertook development of both a coincident composite and a leading composite economic index. The ***Coincident Composite Index*** is a construct of business cycle indicators that is used in describing current general economic conditions. The ***Leading Composite Index*** is a construct of leading business cycle indicators that is used in forecasting economic conditions eight to ten months in advance. The Coincident and Leading Composite Index indicators are listed in Table 1 below. These indexes are constructed specifically for Salt Lake County and are updated bi-monthly and published on the County Auditor's web site at www.slcountyauditor.org.

Coincident Index Components	Leading Index Components
Taxable sales	New vehicle purchases
Manufacturing work hours per week per employee	Total residential construction permits issued
Total non-farm employment	Non-residential construction value
Wholesale & retail trade hours per week per employee	Construction employment
Unemployment rate	Initial claims for unemployment insurance
Aggregate purchasing power	Help-wanted Index
	Local area stock prices
	Local area ten-year yield curve rate

Table 1. *Business cycle indicators included in the Coincident and Leading Indexes.*

In Figure 1 below, the **Coincident Composite Index** for the County is summarized from January 2001 to September 2005. This index shows that the Salt Lake County economy is experiencing robust growth.

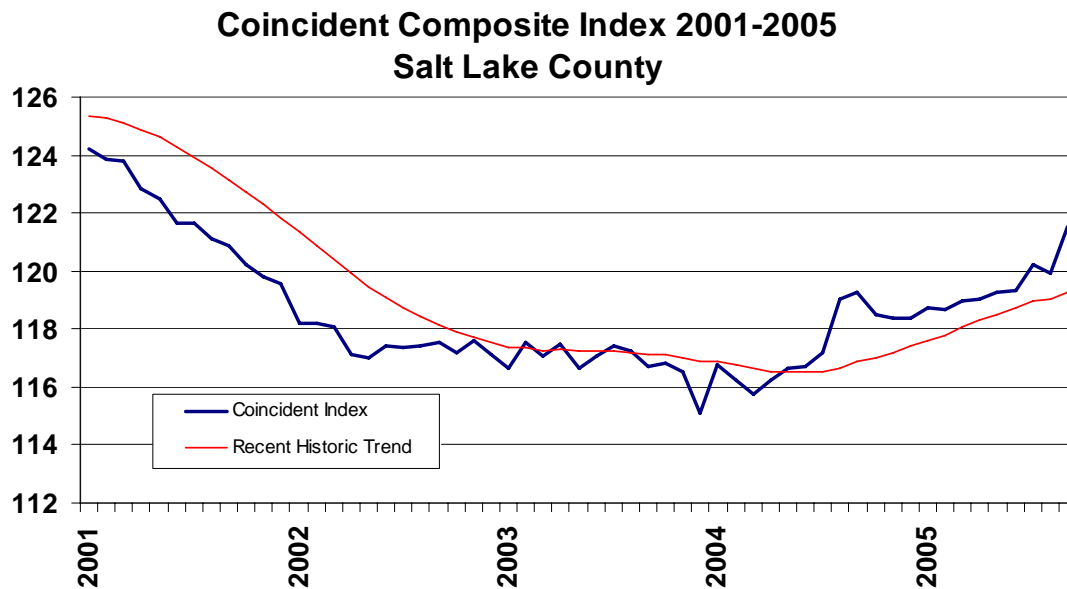


Figure 1. The Salt Lake Coincident Index has been performing above its recent historical trend, and has shown consistent growth since May 2004. 1992 was selected as the base year, where average Index value of 1992 = 100. The “Recent Historical Trend” line is a 12-month moving average for this index.

The **Leading Composite Index** is presented in Figure 2 below. Based on the continued upward trend in this index, we expect continued robust growth throughout 2005 and into the first half of 2006.

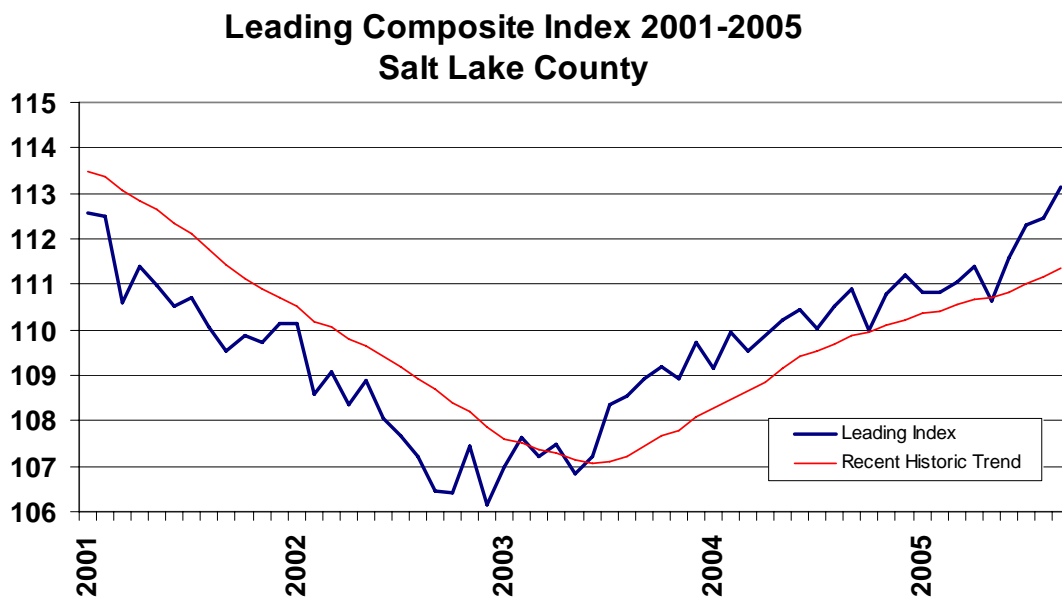


Figure 2. The Salt Lake County Leading Index has outperformed its recent historical trend since June 2003. Moreover, consecutive month-over-month increases, in the index, between May and September 2005 suggest that the County’s economy will continue to show strong growth into at least the first half of 2006. 1992 was selected as the base year, where average Index value of 1992 = 100. The “Recent Historical Trend” line is a 12-month moving average for this index.

The labor market expansion, which is represented in Figure 3 below, continues to play a significant role in the County's economic growth. Here the number of initial claims for unemployment insurance is compared against the Salt Lake Metro-area help-wanted index. This strong recovery is indicated by the sizable divergence between these two leading indicators, starting in October 2003.

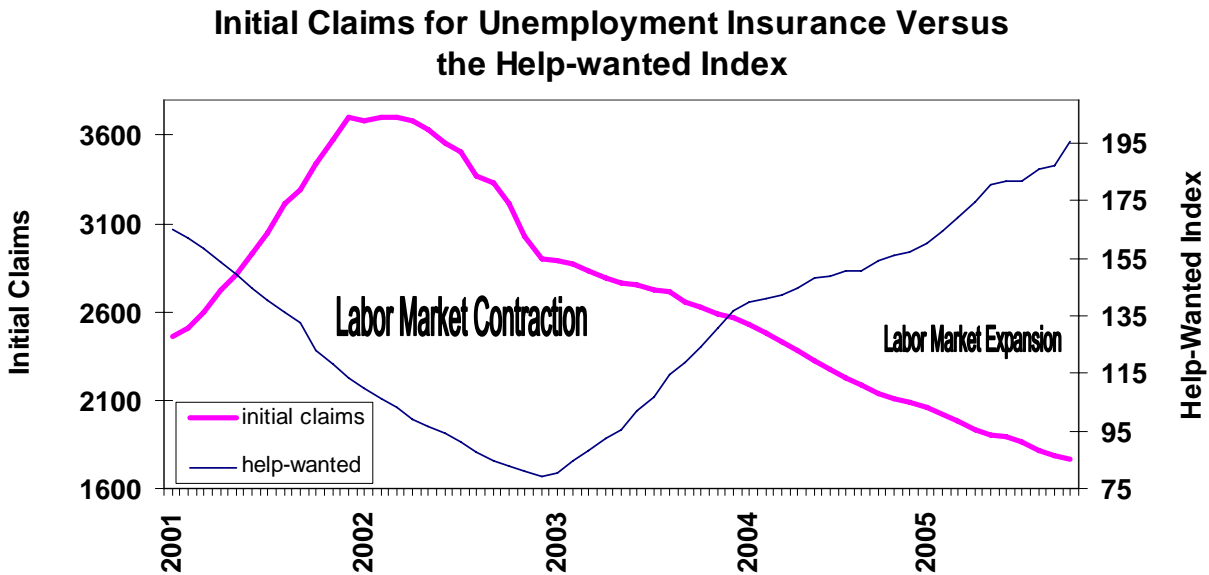


Figure 3. *The widening gap between the rising help-wanted index and plummeting initial-claims indicates a strong labor-market expansion.*

In addition to the factors defined in the indexes, recent increases in housing prices in the valley may add fuel to the expansion of economic activity as consumers' and households' paper wealth appreciates.

Budget Overview

Salt Lake County's total Recommended Budget for 2006 for all funds is approximately \$828 million. Included in this amount are the budgets for the County's 12 internal service funds which are used primarily to account for the financing of services provided by one County agency to other County agencies (rather than to the general public). These services are provided on a cost reimbursement basis. After adjusting the overall budget for these internal charges and other interfund charges, the total Recommended Budget for 2006 is approximately \$644 million (net budget).

The 2006 Recommended Budget includes proposed expenditures for a number of County programs such as public safety, human services, public works, and various other programs. More specific information on the allocation of the County's budget is presented in Figure 4 on page 4. Budgeted revenues are presented by source in Figure 5 on page 4.

2006 Recommended Budget

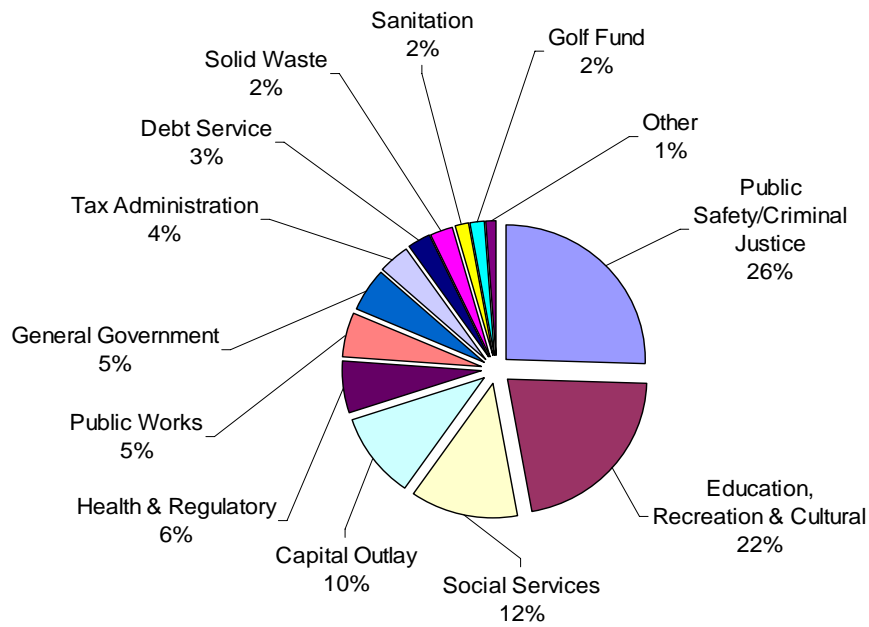


Figure 4. 2006 Recommended Budget allocated to major Salt Lake County program categories.

2006 Recommended Budget Revenues

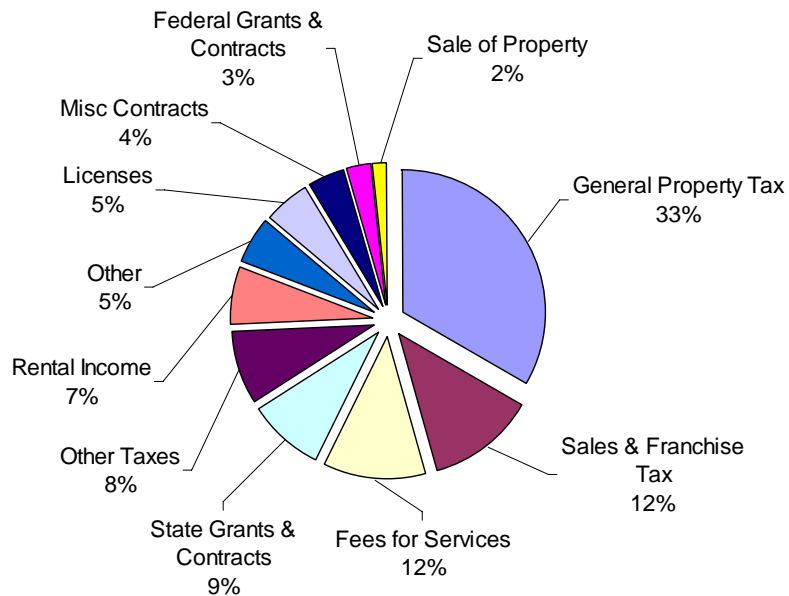


Figure 5. 2006 Recommended Budget - Revenues by major source.

Major Issues and Initiatives

The 2006 Recommended Budget is the culmination of several on-going initiatives and includes the following:

- 1. Jail Budget and Alternatives to Incarceration.** The Sheriff's 2006 budget request for the Jail was \$65.9 million (in the Tentative Budget) and included a request to reopen the Oxbow Jail in addition to maintaining existing operations at the Adult Detention Center. Funding to reopen the Oxbow facility was not included in the Mayor's Proposed Budget nor was it restored in the Council recommended budget. The Council recommended budget for the jail also includes a reduction for the Adult Detention Center operating budget. The Council recommended budget for the Jail is \$54 million which is \$1.2 million less than the 2005 adopted budget. Furthermore, the Council added specific legislative intent that the Sheriff close five housing units (approximately 300 beds) in the Adult Detention Center during 2006 for the purpose of limiting the types of prisoners accepted by the Jail. The Council has approved funding for the Mayor's Alternatives to Incarceration initiative in Community Resources and Development, Criminal Justices Services, Mental Health, the Sheriff's Office, and Substance Abuse Services.
- 2. Salt Palace Convention Center Expansion.** The 2006 Recommended Budget includes continued funding for the Salt Palace Convention Center expansion. The total construction budget for this expansion is \$61 million which is necessary to meet the exhibit and meeting space requirements of large conventions. In 2004, the County issued \$14.7 million in sales tax revenue bonds to finance the costs associated with the first phase of the project. Earlier this year, the County issued an additional \$57 million in sale tax revenue bonds to finance the second phase of the project and a parking structure at the South Towne Exposition Center. Additionally, the State of Utah and Salt Lake City contributed \$4 million and \$8 million respectively for the Convention Center expansion.
- 3. South Towne Exposition Center.** The 2006 Recommended Budget includes \$19.7 million for the construction of a multi-story parking structure and other improvements at the South Towne Exposition Center. The parking structure will provide parking for approximately 1,000 vehicles.
- 4. Millcreek Special Improvement District.** The purpose of this project is to construct an infrastructure upgrade which will deliver a minimum water system fire flow of 1,500 gallons per minute and to provide sufficient fire hydrants for all properties within the boundaries of the District. The project will be funded from a \$3.1 million contribution from Salt Lake City, a \$2.5 million fund balance transfer from the Municipal Services Fund, and the proceeds of special improvement district bonds yet to be issued. Approximately \$11 million is included in the 2006 budget for this project.
- 5. Enhanced Budget Reporting Initiative.** To further enhance the relevance of the information provided to policy makers, citizens, and other stakeholders, both the 2006 Tentative Budget and Mayor's Proposed Budget includes a "narrative report" for each elected official's office and each of the divisions within the County's four departments. The reports are intended to provide a comprehensive overview of County government operations and are structured to include the following information:

 - Statement of purpose
 - Description of principal services

- Statutory authority
- Organization goals
- Key outcomes, performance measures, and operating statistics
- Major initiatives, trends, and challenges

These reports are the culmination of a cooperative effort between Council staff, the Mayor's Office, and my staff. The information in each report was gathered to assist policy makers in evaluating budget requests and related policy issues and to improve the quality of financial information provided to citizens and other stakeholders. After the 2006 County budget is adopted, this information will be included in a comprehensive budget document that will be available at www.slcoaud.org.

- 6. Performance Measurement.** A comprehensive performance measurement system is intended to improve the accountability of government to citizens and provide meaningful information to elected officials on program results and effectiveness. Performance measurement systems are used to identify and track output, outcome, and other measures that are relevant to the goals and objectives of each program. In a performance measurement environment, agencies will have the opportunity to demonstrate the results they are achieving towards meeting the needs of this community with the financial resources they have been allocated in their respective budgets.

At the direction of the County Council, the County began a "pilot" implementation of performance measurement in Aging Services and the Surveyor's Office in 2004. During 2005, the Mayor's Office began implementing performance measurement in the Administrative Services, Community Services, Human Services, and Public Works departments. I am pleased to report the progress achieved to this point is very encouraging.

I believe implementation of performance measurement represents a strategic step forward for the County. However, for this initiative to be successful on a long-term basis, sustained political support from the Council, Mayor, and other independent elected officials is critical. Expectations must be realistic. Also, the Council must commit to utilizing the performance data in the appropriation process. It is clear that implementation of performance measurement on a county-wide basis will not be easy and in fact, will be a multi-year undertaking.

Employee Compensation

County employees are our most important asset. We currently have a hard-working, competent career employee group. We need to retain these employees to continue providing citizens with the quality service they deserve. To attract and retain qualified employees, our compensation structure should be competitive.

Employee compensation and benefit costs represent 57% of the total 2006 recommended operating budgets (includes only those budgets with operating programs). The 2006 Council Recommended Budget includes the following compensation package for employees:

- 2% Structure/COLA adjustment
- 2.75% merit increase for eligible employees

- 1% longevity payment to 401(k) accounts of merit employees not eligible for a merit increase
- \$250,000 allocated to the Employee Service Reserve fund for a benefit yet to be defined

This compensation package will cost approximately \$7.2 million in 2006. In addition, the budget includes a 5.5% increase for Sheriff deputies and a 2.75% increase for sergeants at a cost of approximately \$1 million.

A 6.2 % increase for employee health insurance is included in the 2006 budget which will cost an additional \$1.7 million. The employee health insurance plans approved by the Council include deductibles, increased medical and prescription drug co-pays for employees, and other changes. Without these adjustments, the budgeted increase for employee health care costs would have been 15 % in this budget.

The 2% structure adjustment approved by the Council is somewhat below the projected market increase of 2.47% reported in the **2005 Salt Lake Area Compensation Survey**¹. The Bureau of Labor Statistics West Urban Consumer Price Index (CPI) increased 3.11% for the most recent 12 month period data is available. After adjusting the CPI for “substitution bias”² the actual cost-of-living increased by 2.61% during this period. The difference between the Council’s approved structure adjustment and the calculated increase in cost-of-living represents lost purchasing power for employees.

I am concerned about the effects of inflation on our residents and particularly our employees in Salt Lake County this year. While the West Urban CPI is a good indicator of the fluctuation in the price of goods and services in our local economy, it does not take into account the price of purchasing a single family home, which is on a steep upward trend in the valley over the last six to eight months. One would hope housing inflation is somewhat mitigated by the recent increase in national and local interest and mortgage rates, however, Salt Lake County has been recognized nationally as a market with undervalued housing prices that are now just beginning to adjust to national averages. This could cause speculators to enter our market which would accelerate such an adjustment. The increase in local housing prices paired with the recent increase in interest rates can create inflationary pressures on both our local population and employees that would not necessarily be fully reflected in a Cost of Living index derived from the West Urban CPI.

One could argue the annual merit increase, while intended to be an incentive for performance and longevity, can provide some mitigation of these pressures. However, to the extent it provides such mitigation, it ceases to be an incentive, and simply becomes another adjustment to recognize economic forces. The decision rests with the Council, to weigh and consider these issues in determining appropriate services, service levels, and protections provided by this government for our constituency versus compensation packages for our most valuable resource, our human resources.

¹ The 2005 Salt Lake Area Compensation Survey is a detailed study of the compensation practices (including benefits) of 46 mid-size and large employers in both the private and public sectors in Utah.

² The CPI measures only the change in fixed prices over time but does not account for the impact of price changes on the willingness of consumers to substitute among goods and services. In order for the CPI to reflect the true cost of living, an adjustment must be made to offset substitution bias. Empirical research has found that subtracting 0.50 percent from the percent change in the CPI appropriately adjusts for the substitution bias.

Property Taxes

The 2005 Recommended Budget includes a property tax revenue increase for the Salt Lake Valley Fire Service Area Fund and judgment levies for several Countywide funds, the Municipal Services Fund, and the Library Fund. Property tax revenues for all funds are projected at \$181.7 million for 2006 and are summarized by fund in Table 2 below. With the exception of the Salt Lake Valley Fire Service Fund and Judgment Levy funds, property tax revenue increases in other funds in Table 2 represent additional revenue for “new growth” anticipated to occur in the County and does not imply an increase in the tax rate above the certified rate.

Fund	2005 Property Tax Budgeted	2006 Property Tax Projected
General	\$84,514,270	\$87,195,455
Municipal Services	6,755,153	6,550,000
SL Valley Fire Service	15,042,130	16,400,000
Flood Control	4,514,547	4,630,000
State Tax Administration Levy	14,077,621	14,530,000
Library	23,147,341	23,850,000
Health	9,902,878	9,604,545
Governmental Immunity	97,087	99,500
Bond Debt Service	15,048,491	15,425,000
Planetarium	1,941,741	1,990,000
Municipal Svcs Judgment Levy	0	59,115
State Tax Adm Judgment Levy	0	143,334
Library Judgment Levy	0	127,858
County-wide Judgment Levy	0	1,056,439
Total Property Tax Revenue	\$175,041,259	\$181,661,246

Table 2. 2005 & 2006 Property Tax Revenue by Fund

The Financial “State of the County”

As the chief accounting and budget officer of Salt Lake County, I am also including in this budget message my comments and observations on the financial “state of the County”.

Bond Ratings. Bond ratings are one of the most important indicators of government financial performance. Salt Lake County has the highest possible bond rating (for general obligation debt issues) and the lowest cost of borrowing in the nation. From a total of 3,033 counties, Salt Lake County is one of 21 counties in the nation that have a simultaneous triple ‘A’ credit rating with Moody’s Investors Service, Standard & Poors, and Fitch Ratings. The County’s exemplary bond rating translates into significantly reduced interest costs for our taxpayers.

Minimum Financial Reserves. Maintaining a minimum reserve in County funds is a financial management “best practice” and is critical to retaining the County’s AAA bond rating.

The 2006 Recommended Budget includes sufficient reserves for the General Fund, Municipal Services Fund, and several of the County's other governmental funds.

Long Range Revenue and Expenditure Projection. In Salt Lake County for a number of years our budget decisions have included not only the current year impact, but a **five-year view** of the consequences of our decisions. A multi-year financial forecast alerts elected officials and executive management of potential budget stress which may result from projected revenue and expenditure imbalances. Multi-year budget and revenue planning is another financial “best practice” tool the County should continue to utilize and in fact, is a significant factor cited by both Standard & Poors and Fitch Ratings in evaluating state and local government credit worthiness.

Certified Property Tax Rate. The certified property tax rate is intended to allow local governments to collect the same amount of revenue as was received in the prior year plus additional revenue for “new growth” which occurs as new homes are built or new businesses move into the area. Property tax revenue collected from new growth is intended to assist in paying for the cost of services provided in the areas where the growth occurred. However, under current law governing property taxes in Utah, the certified tax rate is not adjusted for the effects of general inflation. Over time, the purchasing power of property tax revenues collected is diminished and it may become necessary to eliminate selected programs and reduce service levels in others or “raise” taxes to keep up with inflation.

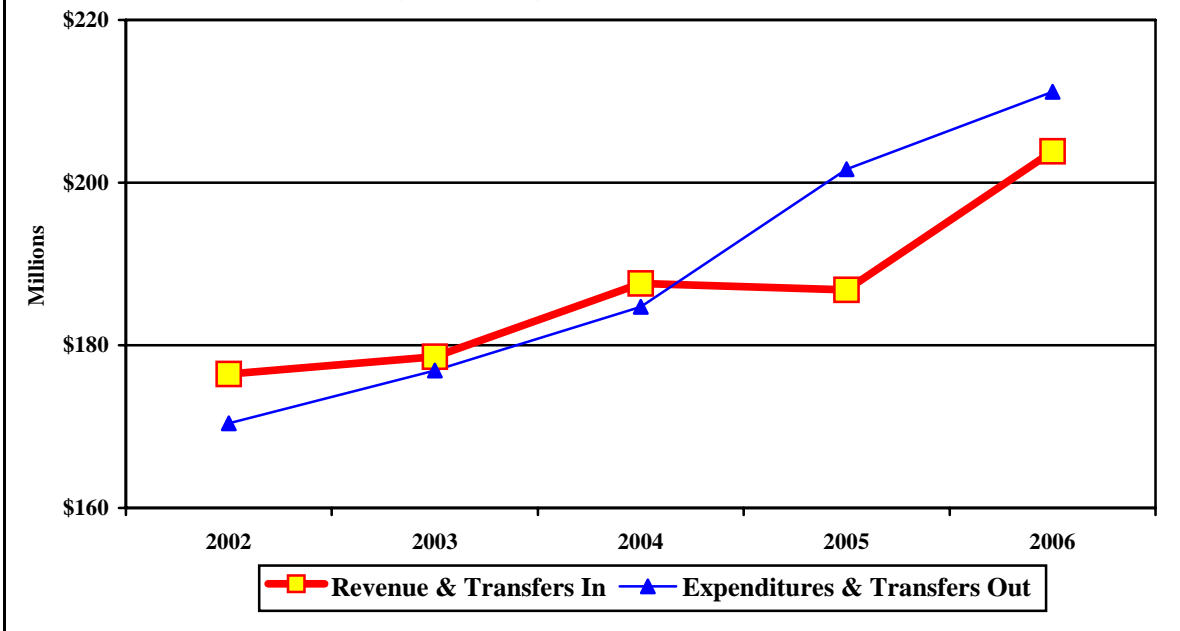
Ultimately, we must recognize that political and social philosophy, or rather, the services, protections, and or facilities, that the representatives of the people, the Council, deem necessary, appropriate, or prudent to provide through County Government to its constituents, drive the need for funding and matching fiscal operations and philosophy. When the average citizen hears the term “tax increase” they are left with the impression that their government has determined to provide additional services, an increased level of services, or additional protection.

In Utah that is not necessarily the case. Under Utah law, adjustments for inflation are considered a tax increase, and it is incumbent on us to notify the public of such. This has led to a historical philosophy in the County of conducting major inflationary and/or service level adjustments every five to ten years, resulting in what appears to be large tax increases. To be fair, it has also resulted in relatively low property tax rates when compared to national averages. These low property tax rates undoubtedly stimulate additional local economic activity in addition to heightened liquidity in our real estate sectors. One might argue it would be more acceptable to the taxpayers if we simply adopted a philosophy of adjusting for the CPI every year, except in years where we can or desire to implement real government service level or program cuts or expansion to cover the rising costs of goods, services, and our human resources.

Structural balance in the General Fund. For the past three years, actual revenues and recurring incoming fund balance transfers have exceeded expenditures and recurring fund balance transfers out in the General Fund. This structural balance is important to the long-term fiscal health of the County and is a direct result of conservative budgetary and other financial policy decisions made by the Mayor and Council. However, for both 2005 and 2006, current year budgeted expenditures and recurring fund balance transfers out exceed current year revenues and recurring fund balance transfers into this fund (see Figure 6 on page 10). This trend is not readily apparent because of the creation of the Grant Fund in 2001 and the associated fund balance transfer each year from the General Fund. For the 2006 Recommended Budget, the budgeted transfer from the General Fund is \$21.9 million which is the planned level of county funding to be included with specific grant revenues received by the County (for delivery of human services programs). This budgetary imbalance should be substantially mitigated by increased revenues as our economy continues to improve and by budgetary underexpend.

Revenue vs. Expenditures General Fund

(including Recurring Fund Balance Transfers)



	2002	2003	2004	2005	2006
Revenue & Recurring Transfers In	176,464,035	178,602,503	187,595,432	186,829,000	203,838,562
Expenditures & Recurring Transfers Out	170,428,576	176,901,147	184,747,619	201,646,093	211,134,366

Figure 6. Actual revenues and recurring fund balance transfers in have exceeded actual expenditures and recurring fund balance transfers out from 2002 to 2004. Budgeted expenditures and recurring fund balance transfers out exceed revenues and recurring fund balance transfers in 2005 and 2006.

Matching current year expenditures with current year revenues on a budgetary basis is difficult. The downward bias in the certified property tax rate will invariably reduce the weighted average revenue growth rate to an amount that is often less than historical expenditure growth. This effect is particularly exacerbated during an economic downturn as sales tax revenues level off. However, based on our most recent **Long Range Revenue and Expenditure Projection** for the General Fund, the current revenue and expenditure trend should be sustainable through 2009 without invading minimum reserves and jeopardizing the County's bond rating. Projected ending undesignated fund balances and minimum reserves are summarized in Figure 7 on page 11.

911 Revenues. All 911 revenues collected from the unincorporated County are currently remitted to the Valley Emergency Communications Center (VECC) to pay for the cost of 911 call taking services. VECC provides Emergency 911 call taking and dispatch services to member cities in Salt Lake County and the Unified Fire Authority. Total 911 revenues from the unincorporated County are projected to be \$1.5 million in 2006. During a recent review of VECC's financial records, we noted that 911 revenues continue to be used to subsidize police and fire dispatch services for VECC members. I am concerned that unincorporated County residents may be financially subsidizing dispatch services to VECC members. I support the

Council's stated legislative intent to redirect 911 revenues from VECC to the County to protect the interests of citizens in the unincorporated County.

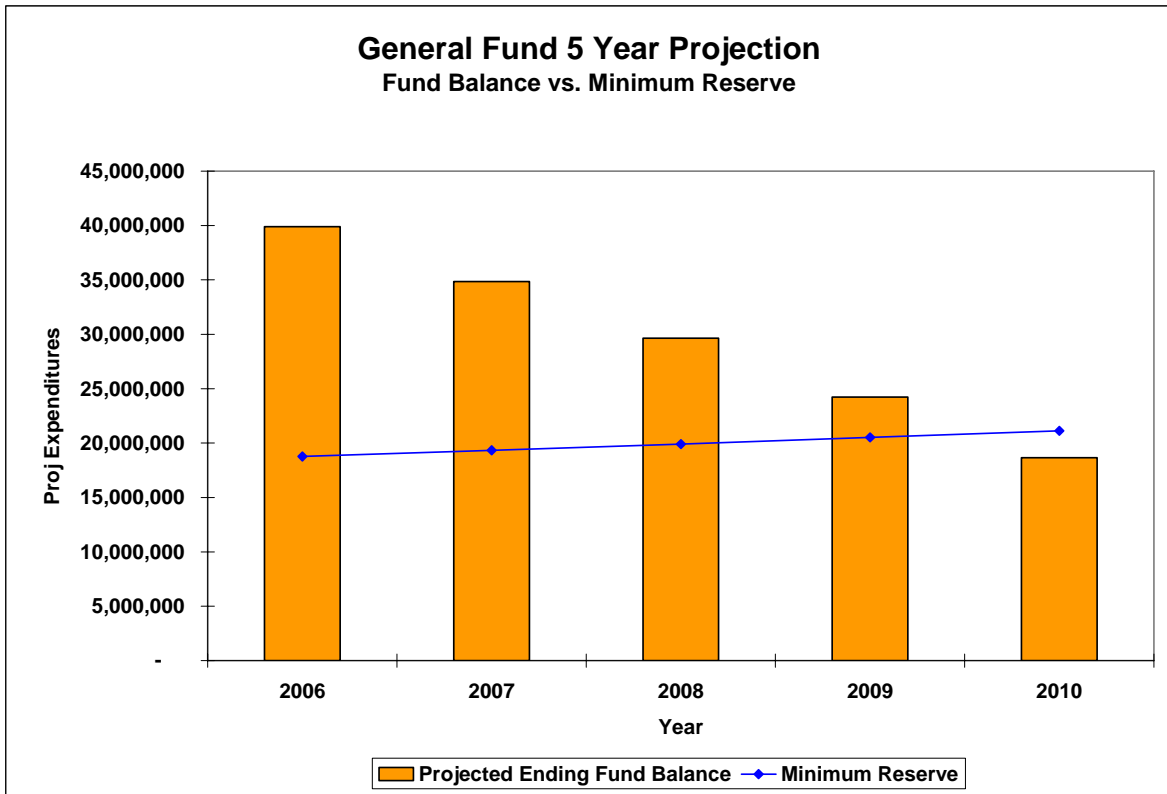


Figure 7. 5-year projection of General Fund year-end fund balance compared to the required minimum fund balance to maintain the County's triple AAA bond rating. Fund balances are projected to dip below the minimum reserve in 2010 without management action.

Redevelopment Agency (RDA) Reform. In this year's legislative session, a moratorium was issued on new RDA's to allow time to study whether material amendments to the law would be appropriate. I have previously briefed the Council about the Smart Redevelopment proposal that my office supports to amend current RDA laws. The idea has received positive feedback, but we have reason to believe that Smart Redevelopment will only be added as a "fourth track" to legislation currently being promoted by the Utah League of Cities and Towns, which has proposed three other tracks. The League's proposal appears to have support at the legislature and there is a strong likelihood that it will become law.

The three tracks promoted by the League allow municipalities to use property tax increment financing to fund redevelopment projects. Property tax increment financing under this legislation would result in indirect subsidies being paid to each redevelopment district from taxpayers of overlapping taxing entities. As such, I am concerned about subsidies paid by residents of the unincorporated County and of cities that do not have RDAs. Cities have historically used these subsidies to build retail establishments that may provide no benefit to residents who are subsidizing their development. There are strong indications that the pace at which residents are subsidizing retail developments in other cities will significantly accelerate after passage of the new bill.

While I strongly oppose the subsidies that exist under current RDA legislation and that will likely continue under the new legislation, I feel obligated to point out that the best way this

Council could protect the financial interests of unincorporated residents is to aggressively pursue any and all RDA, EDA, and CDA opportunities in the unincorporated county. The only way to offset subsidies being paid by residents of the unincorporated County is to draw subsidies into it through new RDA, EDA and CDA projects in the unincorporated county. Of course, some of these subsidies will be paid by residents of incorporated cities.

I personally abhor the institutionalization and perpetuation of a zero sum game where neighboring communities fight for retail projects, and do it with subsidies from outside their community, but this is the incentive that exists under the State's tax laws. And right or wrong, municipalities that take advantage of the current laws stand to benefit at the expense of municipalities that do not. As representatives of the residents of the unincorporated County, I believe we have a responsibility to mitigate the negative financial impacts of subsidies they currently pay, and to secure benefits of the law for them.

Thankfully, while strong incentives will exist for cities and counties to pursue RDA opportunities, it appears eminent domain will be excluded as a tool in the new legislation. We are hopeful that our own proposal for RDA reform will also be passed into law in some form, and in future years as the legislature is made aware of the realities of this zero sum game, will default to the system we have proposed as the only funding mechanism cities use for redevelopment, economic development, and community development.

Summary and Closing Remarks

The financial state of Salt Lake County is sound. Our fund balances are healthy and we have the highest possible bond rating for our general obligation debt. Implementation of the Council's performance measurement initiative will improve the quality of information available to policy makers and will ultimately improve the accountability of this government to citizens. We continue to move towards a robust and open dialogue between the Auditor, Mayor, and Council on fiscal matters. This public airing of budget issues is one of the benefits citizens can expect to receive from this form of government.

I commit the resources of my office to continue working closely with the Mayor, Council, and other Elected Officials. I will be happy to provide further documentation, information, or to answer any questions from the citizens here this evening.