BUFFALO FISCAL STABILITY AUTHORITY

First Annual Report
Fiscal Year 2003-04

October 2004

Buffalo Fiscal Stability Authority

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Executive Summary

September 2004 marks the first anniversary of the inaugural four-year Financial Plan of the City of Buffalo and its covered organizations, submitted in accordance with the Buffalo Fiscal Stability Authority Act of 2003. The Buffalo Fiscal Stability Authority (BFSA) was established to address the fiscal instability in the City of Buffalo and its covered organizations without a reliance on annual extraordinary increases in State aid. During its first year, the BFSA helped the City and covered organizations begin the road to long-term structural budget balance.

The strategy to achieve fiscal stability is multi-pronged, built on multi-year financial planning; strict fiscal discipline; formal monitoring and reporting mechanisms; and implementing actions that achieve recurring cost savings and generate increased revenues. Despite progress made to date, the long-term structural balance of the City remains tenuous. In order to continue the steps initiated in BFSA's first year, the reform-oriented partnership that has developed among the Authority, the City, its covered organizations and New York State must continue and strengthen.

Landmark actions taken by the Authority, the City and its covered organizations in this critical first year of BFSA's responsibilities include:

<u>Multi-year Financial Planning:</u>

- Approved the inaugural four-year Financial Plan for the City of Buffalo, Buffalo Public Schools, Buffalo Urban Renewal Agency and Buffalo Municipal Housing Authority, which identified future budget shortfalls and mapped recurring gap closing measures to achieve structural balance.

- Worked with the City Comptroller's Office and Buffalo Public Schools to refine the accuracy of historical cash flow reports and improve forecasting to enhance appropriate investment of cash reserves and overall money management; better gauge cash flow needs; and appropriately size short-term borrowings.

- Coordinated with external auditors of City and covered organizations in completion of year-end audits, and monitored reforms to address process issues raised in recent management letters.

- Approved the second four-year Financial Plan for the City and covered organizations, developing gap-closing strategies for fiscal years 2005-2008.

<u>Monitoring Fiscal Health</u>

- Created monitoring mechanisms to improve financial tracking, enhance long-term planning and facilitate dialogue among the City, covered organization leaders and BFSA.

- Imposed a wage freeze on the City and its covered organizations effective April 2004, enabling a balance of the second four-year Financial Plan by generating aggregate savings of more than $6 million in 2004-05; $9 million in 2005-06; $12 million in 2006-07 and $13 million in 2007-08. The freeze minimized layoffs and preserved essential services.

- Initiated a quarterly reporting process by the City and its covered organizations to review financials and monitor implementation of gap-closing measures.

- Began an interim accrual-based reporting process in the City and covered organizations to more accurately track changes in year-end fund balances.

- Encouraged revision of the City's "salary ordinance" practice of assigning jobs, in favor of a process that more closely ties workforce counts to budgeted funds.

- Reviewed 126 School District contracts, obligations and settlements worth more than $103 million, and 170 City contracts, obligations and settlements worth more than $99 million.

- Advocated for a national search for, and hiring of, a Chief Financial Officer in the Buffalo Public Schools.

<u>Right-Sizing the Workforce</u>

- Imposed a City hiring freeze in December 2003.

- Monitored the reduction of the City workforce by 256 positions between July 1, 2003 and the end of the fiscal year.

- Monitored the Buffalo Public Schools' reduction of its budgeted workforce by 645 in fiscal year 2004, and encouraged maximization of classroom teacher presence.

- Tracked the Buffalo Urban Renewal Agency's workforce reduction by 26 positions, along with 8 additional reductions in BURA-related activities.

<u>Improving the Outlook on City Debt</u>

- Facilitated a revised outlook on City debt from Standard & Poor's, in which the creation of BFSA and development of a Financial Plan for structural balance are cited as reasons for removal of the negative outlook.

<u>Developing BFSA's Financing Framework</u>

- Created the legal and financial framework for BFSA debt issuance.

- Completed technical amendments to the BFSA Act to enhance market access and strengthen BFSA's financing mechanism while protecting the City's property tax capacity.

- Successfully launched BFSA's debt issuance program at ratings of AA- from Fitch and Aa3 from Moody's, compared to the City's long-term debt rating of BBB-.

- Completed the inaugural sale of BFSA deficit bonds for the City's 2003-04 ($7.811 million) and 2004-05 ($19.045 million) budgets.

- Sold $84 million in Bond Anticipation Notes, Series 2004A-1, in September 2004 to cover cash flow borrowings for 2004-05. The sale amount was down from $120 million in 2003-04. It received the highest ratings from Moody's (MIG 1) and Fitch (F1+), and did not require letter of credit support, which cost the City approximately $800,000 in its 2003 cash flow borrowing.

- Approved City debt issuances for short-term cash flow borrowing ($120 million in September 2003); refinancing of existing debt on the HSBC Arena ($10.285 million in January 2004); and capital needs ($18.261 million in May 2004).

Implementing Structural Reform and Identifying Savings Opportunities

- Encouraged agreement between City and employee bargaining units comprising approximately 2,000 employees to utilize a single health insurance carrier, saving $6 million in 2004-05 without sacrificing employees' benefit levels.

- Established the City-County Working Group as a forum to facilitate dialogue on cost-saving collaborations between the region's two largest governments, resulting in a consolidation of the City's Parks Department with Erie County, generating $3.4 million in savings and reducing the City's workforce by 61 full-time employees.

- Monitored the School District's commencement of its first-year school closure plan, yielding two closings and two suspensions of service in September 2004; two closings in late fall 2004; and two closings and one suspension of service in winter 2004.

- Facilitated the cancellation of a $57,000 State Department of Labor fine for violations at the City's Department of Public Works.

Informing the Public

- Sponsored two public input forums on the Financial Plans of the City and covered organizations, and established a website to disseminate Authority reports, press releases, meeting schedules and minutes.

- Conducted seventeen public meetings of the Board through September 2004.

<u>Building an Organization</u>

- Developed BFSA's physical, administrative and human resource infrastructure to carry out the responsibilities required by the BFSA Act. Through New York State assistance and contributions, furniture and technology equipment were put in place and functioning at low cost, and within a three-week timeframe.

- Hired a staff of full-time professionals:

  Dorothy A. Johnson, M.S., *Executive Director*, former principal budget examiner for local government affairs in the New York State Division of the Budget and former investment officer in the Office of the State Comptroller;

  Darryl McPherson, Esq., *Chief Counsel*, former Deputy Corporation Counsel for the City of Buffalo Department of Law, with almost a decade of municipal and legislative experience;

  Bertha H. Mitchell, MBA, *Chief Financial Officer*, former Vice President and Senior Credit Officer for Corporate Banking at a major U.S. and Canadian bank, with additional experience in valuations and venture capital activities;

  Dr. Joseph V. Stefko, *Principal Analyst*, former Senior Research Associate for government management and economic analysis at the Center for Governmental Research, a Rochester-based public sector management consulting firm, who holds a doctoral degree with urban policy specialization;

  Robert M. Tocker, M.A., *Associate Analyst*, former Senate Finance and Fiscal Studies Fellow and legislative analyst with the New York State Senate Finance Committee; and

  Heidi Santos, *Administrative Assistant*.

- Rented space through the Buffalo Economic Renaissance Corporation, to circulate funds back for City economic development.

- Adopted and managed BFSA's first budget of under $1 million.

- Adopted procedures relating to Records Access and investments.

Much was achieved in the first year of the Buffalo Fiscal Stability Authority. The City and covered organizations, in conjunction with BFSA, developed Financial Plans that seek to close structural budget gaps through the implementation of actions that produce recurring savings. Tracking mechanisms were put in place to ensure the City, its agencies and the Authority can effectively monitor budgetary performance during the fiscal year. Financing mechanisms were established to allow the City an opportunity to incrementally close its budget gaps while implementing long-term cost savings. And BFSA established the reporting standards and formats the City and its agencies will employ in the coming years to regularly monitor their fiscal health.

A significant amount of work remains, however. Among the issues that must be addressed in the coming year are:

- growing baseline gaps in the City and School District;
- open labor contracts;
- rapidly increasing health expenditures without employee cost sharing;
- obsolete and wasteful contract provisions;
- precariously low fund balances;
- ineffective management controls throughout the system;
- highly speculative revenues in the Financial Plan's out-years; and
- Fire Department restructuring.

State law has weakened the ability of Buffalo to effectively control local costs. Local officials developed a balanced Financial Plan in order to address the City's solvency under current State-mandated limitations. Nonetheless, the Financial Plan of the City and School District includes a growing amount of speculative assumptions in the out-years. BFSA does not have the power to void contracts or portions thereof. State action is essential to remove major constraints to City reengineering and restructuring. In particular, BFSA has noted that the following laws significantly impede long-term structural balance in the City: the Taylor Law (which establishes impasse negotiation procedures including binding arbitration); the Triborough Amendment (which continues the terms of expired contracts indefinitely); and the Wicks Law (which increases the cost of City building projects, like the new firehouses).

These provide generous (and for the City, unaffordable) protections to municipal workers that raise costs beyond local control and hinder negotiations that might otherwise lead to changes in excessively expensive and inefficient contract provisions. Since labor-related costs represent more than three quarters of all spending – and the cost of the average City employee has risen 8 percent, or $5,366 from 2003-04 to 2004-05 – these reforms are essential to long-term management control and fiscal stability without a continued reliance on increasing amounts of State aid or local tax and fee increases.

A continued collaborative approach to addressing the City's budgetary issues is essential for long-term fiscal stability.

Introduction

This is the first annual report of the Buffalo Fiscal Stability Authority, covering the first fiscal year in which the City of Buffalo and its covered organizations operated under the requirements of the Buffalo Fiscal Stability Act. It covers the period through September 2004.

The Buffalo Fiscal Stability Authority Act, which created the Buffalo Fiscal Stability Authority (BFSA), was signed into law by Governor George E. Pataki in July 2003. BFSA was created in response to a State Comptroller's assessment and report, and a determination by the State legislature that the City of Buffalo was faced with a severe fiscal crisis that could not be resolved without State assistance. The City had repeatedly relied on extraordinary annual increases in State Aid to balance its budget, and the State concluded that it could no longer take such actions on the City's behalf. Declaring the maintenance of a balanced budget by the City of Buffalo a matter of overwhelming State concern, the Legislature passed, and Governor signed, the Buffalo Fiscal Stability Authority Act on July 3, 2003.

The BFSA Act, enacted with broad bipartisan support in the New York State Legislature, provided for the following steps to return the City of Buffalo to fiscal stability:

- Created the Buffalo Fiscal Stability Authority as a fiscal control agency over the City and its covered organizations;

- Required the annual development of a four-year Financial Plan for the City and its covered organizations, and vested BFSA with the power to ensure compliance with that Plan;

- Granted BFSA the power to deficit finance for the City and its covered organizations over a four-year period, provided that recurring actions are taken to close increasing percentages of budget gaps each year;

- Developed a highly rated borrowing structure to reduce City borrowing costs; and

- Empowered BFSA to impose financial control mechanisms if the City and its covered organizations cannot operate in accordance with an approved Financial Plan.

By force of the BFSA Act, the Authority was granted "control powers" over the City and covered organizations from its inception. During the control period, the Authority has a wide range of powers, including the power to limit spending of the City or any covered organization; impose a hiring and/or wage freeze; and review and approve any contract, obligation or collective bargaining agreement entered into by the City or any covered organization. The control period will terminate once the City has achieved three sequential balanced budgets without deficit financing assistance from the Authority, at which point the City would operate under an *advisory period*. However, if the City should at any point incur a budget deficit or lose access to the financial markets, a control period would be reimposed for a period not beyond June 30, 2037.

Governance of the Fiscal Stability Authority

The Authority is governed by nine Directors. Seven are appointed by the Governor, one of which upon the recommendation of the State Comptroller, and one of which upon the recommendation of the leaders of the State Assembly and State Senate. The Mayor of the City of Buffalo and the County Executive of Erie County serve in *ex officio* capacities. The Governor designates the chair and vice-chair of the Authority. The following individuals served as Directors of BFSA in its first year:

Thomas E. Baker, Chairman
Mr. Baker the President of The John R. Oishei Foundation and former managing partner of the Buffalo office of a national accounting firm.

John J. Faso
Mr. Faso is a Partner at Manatt, Phelps & Phillips LLP, a law and consulting firm, and former minority leader of the New York State Assembly.

Hon. Joel A. Giambra
Mr. Giambra is Erie County Executive.

Hon. Anthony M. Masiello
Mr. Masiello is Mayor of the City of Buffalo.

H. Carl McCall, Treasurer
(Recommendation of the State Comptroller)
Mr. McCall is former New York State Comptroller and President of Convent Capital.

Ronald M. Pirtle (Served until December 2003)
Mr. Pirtle is Vice President of Delphi Corporation

Rev. Richard A. Stenhouse (Appointed March 2004)
Rev. Stenhouse is the Pastor of Bethel AME Church, Executive Director of Bethel Head Start and a member of the Board of Regents at Canisius College.

Richard Tobe, Secretary
(Recommendation of the State Legislature)
Mr. Tobe is Vice President for Programs at the Community Foundation for Greater Buffalo, a community trust dedicated to improving life in Greater Buffalo, and former economic development chief under former Erie County Executive Dennis Gorski.

Alair Townsend, Vice Chair
Ms. Townsend is Publisher of Crain's New York Business *and former New York City Budget Director and Deputy Mayor for Finance and Economic Development.*

Robert G. Wilmers
Mr. Wilmers is President and CEO of M&T Bank Corporation.

The first meeting of BFSA Directors took place on July 15, 2003. Through September 2004, BFSA has held 17 public meetings of its Directors, including two meetings each in September and October 2003, and May 2004.

2003-04 Fiscal Year in Review

City of Buffalo

The 2003-04 fiscal year was the City of Buffalo's first under a financial control board, and September 2004 marks the one-year anniversary of the City's first Four-Year Financial Plan submission.

The City submitted its first four-year Financial Plan to BFSA on September 2, 2003. That Plan identified significant and growing baseline budget gaps over the next four years, and proposed a strategy to eliminate increasing percentages of the gap each year in accordance with the BFSA Act. On September 15, 2003, at the fourth meeting of the Board of Directors, BFSA disapproved the City's Financial Plan submission on the basis that it was generally incomplete; included unreasonable and highly speculative revenue assumptions regarding sales tax sharing; and lacked a required “declaration of need” for deficit financing. In concluding that the City’s Financial Plan did not comply with the requirements of the BFSA Act, the Board of Directors ordered its revision.

On October 1, 2003, the City submitted a revised four-year Financial Plan to BFSA. To comply with BFSA requirements, the revised Plan reduced workforce levels; removed speculative wage increases (i.e. raises not yet contractually agreed to); mitigated the risk of including speculative sales tax revenues in the Plan, by reducing the assumed amount and moving the assumption into the third year of the Plan; and included BFSA deficit financing to close the remainder of the City’s 2003-04 budget gap. At its October 7, 2003 Directors’ meeting, however, BFSA determined that the Plan still lacked a “declaration of need” for deficit financing and therefore was still not in compliance with the BFSA Act. On October 16, 2003, the City submitted its revised, completed Plan and declaration of need in accordance with the conditions set by BFSA. The Authority’s Board of Directors met on October 21, 2003, to approve the first four-year Financial Plan for the City of Buffalo and its covered organizations.

The City’s Financial Plan called for a staff reduction of 195 in the first year, shrinking the originally budgeted level (pre-BFSA) from 2,894 to 2,699 (Based on numbers provided by the City at the end of the fourth quarter, the workforce contracted by 256 positions between July 1, 2003 and June 30, 2004). A fire reengineering initiative called for the closure of three companies during the year, along with a staffing reduction of 43 firefighters. Over the four years of the Plan, the fire department reengineering was projected to save $1.3 million in fiscal year ending (FYE) 2004, and $4.2 million, $9.6 million and $11.2 million in the three succeeding years. A series of functional mergers with Erie County – including assessment, audit, collections and parks – was projected to yield savings beginning in 2004-05. Additional County sales tax sharing was assumed to produce more than $10 million in new revenues beginning in 2006, growing to $21 million in FYE07. To close the remainder of the City’s gap, a total of $37.6 million in BFSA deficit financing assistance was assumed into the City’s Plan over the period 2003-04 to 2006-07.

Since the BFSA-approved Financial Plan was not implemented until October, the City’s first quarter did not show savings from the gap-closing measures provided for in the Plan (e.g., layoffs and fire department reengineering would not begin until November). As a result, performance relative to the modified budget in the first quarter was poor. The City’s first quarter report to BFSA revealed a shortfall of $2 million above any deficit financing, due in part to overspending in several departments. A number of departments were projecting full-year shortfalls. Police Department operations were projected at $2.5 million over-budget; the Fire

Department at $1.7 million over-budget; and Public Works at $0.9 million over-budget. As a way to mitigate the budget shortfall, BFSA ordered implementation of a hiring freeze on the City effective December 15, 2003.

During the fiscal year's second quarter, the first under the BFSA-approved Financial Plan, the City made some progress against its increased budget shortfall. The City narrowed the projected year-end gap to $0.2 million by drawing down nearly $4 million in FYE02 fund balance and increasing its sales tax revenue projection by $1.8 million. BFSA warned, however, that "the two primary revenue sources which have been relied upon to cover underperforming revenues and overspending in the current year budget are not likely to be available in 2004-05," noting that fund balance was being depleted and sales tax projections for FYE05 already incorporated more reasonable growth factors than FYE04's budget. On the spending side, overages from the first quarter were by-and-large reined in as scheduled layoffs occurred in accordance with the Financial Plan.

In its third quarter, the City began to realize notable cost savings as a result of the position reductions contained in the Financial Plan. Full-year expenditures were projected at more than $3 million under-budget, and the City was projecting an overall positive variance of $3.4 million. Position cuts had generated substantial savings not only in salaries, but benefits; health insurance and pension costs were both projected under budgeted levels.

Preparations for developing the City's second Financial Plan began in April. In developing the next four-year Plan, due to BFSA in May, several issues of concern surfaced. First, the City requested a Financial Plan modification to eliminate the scheduled layoffs associated with the fire reengineering initiative, claiming that the initiative was now cost-negative in light of exorbitant overtime costs and manpower issues in the department. In terms of cost containment, the fire reengineering initiative had represented the single-largest savings in the original Financial Plan.

Second, the City's preliminary budget projections for the next four years showed a dramatic escalation in the gap going forward, in many instances due to circumstances over which the City has only limited control (e.g., pension costs and health insurance). The projected gap for 2004-05 was $49.6 million, a nearly $20 million (or 63 percent) increase over the FYE05 gap projected in the Financial Plan initially approved by BFSA. Further, the cumulative four-year gap had grown from $140 million to $250 million. In addition, the City received a grievance arbitration decision in mid-April that had the potential to force the re-hiring of some of its blue-collar layoffs, as well as compromise layoff initiatives in the Financial Plan going forward.

Citing all of these factors, BFSA implemented a wage freeze on the City and all covered organizations on April 21, 2004, that was projected to save the City $29 million over the course of its next Financial Plan. The BFSA Act requires the Authority to “periodically evaluate the suspension of salary or wage increases.”

Buffalo Public Schools

The Buffalo Public School District is the single largest “covered organization” of the City of Buffalo. Covered organizations are defined by the BFSA act as any governmental agency, public authority or public benefit corporation which receives or may receive monies directly, indirectly or contingently from the City. As a covered organization, the Buffalo Public Schools must comply with all of the same financial planning and reporting requirements as the City, and are subject to the same financial control powers of BFSA.

The Board of Education’s first four-year Financial Plan was submitted to BFSA with the City’s on September 2, 2003. BFSA considered the Financial Plan wholly deficient and not in compliance with the BFSA Act, in that it did not include complete fiscal information; failed to detail financial impacts of management actions already implemented or planned; lacked a formal and reasonable strategy for closing budget gaps as required by the BFSA Act; and did not address themes of financial mismanagement cited in outside audits, including inadequate oversight; fragmented record-keeping; and poor accountability. Most importantly, the District’s Financial Plan contained the acknowledgement that, “It is the opinion of the Board of Education that this four year financial plan will not meet the basic needs of the students attending schools in the City of Buffalo.” The Fiscal Stability Authority unanimously rejected the Board of Education’s Financial Plan on September 15, 2003, and required its immediate revision.

The School District submitted its revised four-year Financial Plan with the City on October 1, 2003. The revised Plan was a dramatic improvement over the prior month’s submission, in that it contained reasonable revenue and spending assumptions; complete financial information; and a series of recurring actions designed to close increasing budget gaps over the next four years. The reduction of 645 staff positions (as provided for in the District’s 2003-04 budget) and closure of schools were central gap-closing components of the Plan.

The downsizing in staff and school facilities acknowledge declining enrollment trends in the Buffalo Public Schools. State-reported enrollment figures for BPS have fallen by more than 10 percent since 2000, to 41,101 as of October 2003. The loss has been more pronounced in the lower grades, with K-6 enrollment down 18 percent and K-3 enrollment down 21 percent in the same period.

Unlike the City, the first year of the School District's four-year Financial Plan was already balanced, as a result of actions taken in its July adopted budget to close a $37.4 million gap on its $617 million budget ($507 million general fund plus $110 million grants and food service funds). The District's out-years contained gaps, however, projected to grow from $27.7 million in 2004-05 to $31.3 million in 2006-07. The Financial Plan assumed a reliance on $20.1 million in BFSA deficit financing over its final three years.

In the first quarter, the District remained on its full-year budget benchmarks. Through September, employee compensation and benefit costs were better-than-budget, but almost entirely offset by higher than expected charter school payments. At the end of the first quarter, the District was projecting a $33,000 surplus on its $617 million budget. That projection grew to $735,000 by the end of December, as revenues continued running considerably better-than-budget. In the third quarter, a $92,000 deficit appeared due to higher-than-expected employee benefit costs and charter payments. Preliminary year-end numbers show the District with a slight deficit of $0.8 million when prior-year encumbrances are recognized. An operating surplus of $1.0 million is estimated for FYE04-only operations.

The School District began implementing its school closing plan, a major component of the Financial Plan, in the second quarter. A Building Usage Committee made recommendations on school closures, suspensions and facility shutdowns late in 2003, and community meetings on the selected school closings were held between December and January.

Similar to the City, however, the process of developing the School District's Financial Plan revealed troubling trends. Preliminary budget information developed in March reflected an increased budget shortfall for 2004-05. Whereas the BFSA-approved Financial Plan had projected a $27.7 million gap for 2004-05, documents released by the District on March 2, 2004 revised the gap projection to more than $45 million. The largest contributors to the projected gap increase were reduced revenues for the District in the Governor's Executive Budget; a substantial growth in the projected cost of employee benefits, particularly the extremely high-cost "termination pay" (including incentives) for retiring employees; and higher-than-expected charter school payments.

The wage freeze imposed by BFSA on April 21, 2004 saved the District $3.1 million annually, savings which the Board of Education incorporated into its new Financial Plan. The District noted that BFSA's wage freeze action restored some of the 198 classroom teachers who otherwise would have been eliminated under the original Financial Plan.

Other Covered Organizations

The BFSA Act defines covered organizations as "any governmental agency, public authority or public benefit corporation which receives or may receive moneys directly, indirectly or contingently from the City." The Act names the City School District, the Joint Schools Construction Board and the Buffalo Municipal Housing Authority as covered organizations, and grants BFSA the power to name additional covered organizations where appropriate.

In addition to the Buffalo Public Schools, BFSA focused on two other covered organizations during fiscal 2004: the Buffalo Municipal Housing Authority (BMHA) and Buffalo Urban Renewal Agency (BURA). BFSA did not exercise control powers over the Joint Schools Construction Board (JSCB) during fiscal 2004 since the BFSA Act exempted its first issuance of debt, initiated prior to the creation of BFSA, from the first Financial Plan period. BFSA's formal coverage of JSCB begins with the 2005-2008 Financial Plan.

As with the City and School District's initial Financial Plans, the Fiscal Stability Authority rejected the four-year spending plans originally submitted by BURA and BMHA on September 2, 2003. Both agencies were required to submit revised plans, which BFSA approved in October 2003.

BURA's Plan included a strategy to close a projected $2.4 million budget gap in 2003-04, as well as incrementally reduce a multi-year accumulated budget shortfall estimated at $5.4 million. The Plan closed the fiscal 2004 deficit through a combination of staff reductions, lower reimbursement payments to the City, and one-time cuts in Community Development Block Grant programming. The agency's Plan called for paying down the prior-year accumulated deficit between fiscal years 2005 and 2008. Based on preliminary numbers at the end of the fourth quarter, BURA closed fiscal year 2003-04 in balance.

BMHA's Plan projected deficits of $1.1 million in fiscal 2004; $0.4 million in fiscal 2005; $0.2 million in fiscal 2006; and only $152,000 in fiscal 2007. By 2008, BMHA projected its federal housing portfolio (its largest) would finish in annual surpluses. Unlike the other covered organizations, however, BMHA expected reserve monies it is required to maintain by the federal Department of Housing and Urban Development would cover its annual shortfalls. Still, to address areas of financial concern, the Housing Authority's Plan called for transferring units from its State to federal portfolio. Preliminary year-end numbers show that BMHA finished fiscal 2004 with a deficit of $1.6 million, approximately $500,000 worse than its approved budget. As noted above, its cash reserve covered the entire shortfall and stood at $7.7 million at year-end.

Summary of Accomplishments and Actions

The Buffalo Fiscal Stability Authority was created to help restore the City of Buffalo to fiscal health and integrity, so that the City and its covered organizations could continue providing essential services to citizens while meeting obligations to holders of City debt. The Authority's powers and responsibilities fall into two principal categories: fiscal oversight and monitoring, and debt issuance on behalf of the City.

In its first year of operation, BFSA helped the City and covered organizations on the road to long-term structural budget balance. Landmark actions taken by the Authority, the City and its covered organizations in this critical first year of BFSA's responsibilities include:

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- Approved the inaugural four-year Financial Plan for the City of Buffalo, Buffalo Public Schools, Buffalo Urban Renewal Agency and Buffalo Municipal Housing Authority, which identified future budget shortfalls and mapped recurring gap closing measures to achieve structural balance.

- Worked with the City Comptroller's Office and Buffalo Public Schools to refine the accuracy of historical cash flow reports and improve forecasting to enhance appropriate investment of cash reserves and overall money management; better gauge cash flow needs; and appropriately size short-term borrowings.

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- Advocated for a national search for, and hiring of, the first ever Chief Financial Officer in the Buffalo Public Schools.

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- Imposed a City hiring freeze in December 2003.

- Monitored the reduction of the City workforce by 256 positions between July 1, 2003 and the end of the fiscal year.

- Monitored the Buffalo Public Schools reduction of its budgeted workforce by 645 in fiscal year 2004, and encouraged maximization of classroom teacher presence.

- Tracked the Buffalo Urban Renewal Agency's workforce reduction by 26 positions, along with 8 additional reductions in BURA-related activities.

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- Facilitated a revised outlook on outstanding City debt from Standard & Poor's, in which the creation of BFSA and development of a Financial Plan for structural budgetary balance are cited as key reasons for removal of the negative outlook.

Developing BFSA's Financing Framework

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- Completed technical amendments to the BFSA Act to enhance market access and strengthen BFSA's financing mechanism while protecting the City's property tax capacity.

- Successfully launched BFSA's debt issuance program at ratings of AA- from Fitch and Aa3 from Moody's, compared to the City's long-term debt rating of BBB-.

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Implementing Structural Reform and Identifying Savings Opportunities

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- Established the City-County Working Group as a forum to facilitate dialogue on cost-saving collaborations between the region's two largest governments, resulting in a consolidation of the City's Parks Department with Erie County, generating $3.4 million in recurring savings to the City and reducing the City's workforce by 61 full-time employees.

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- Facilitated the cancellation of a $57,000 State Department of Labor fine for violations at the City's Department of Public Works.

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- Conducted seventeen public meetings of the Board of Directors through September 2004.

- Established a website to disseminate Authority reports, press releases, meeting schedules and minutes.

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- Hired a staff of six full-time professionals:

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  Darryl McPherson, Esq., *Chief Counsel*, former Deputy Corporation Counsel for the City of Buffalo Department of Law, with almost a decade of municipal and legislative experience;

  Bertha H. Mitchell, MBA, *Chief Financial Officer*, former Vice President and Senior Credit Officer for Corporate Banking at a major U.S. and Canadian bank, with additional experience in valuations and venture capital activities;

  Dr. Joseph V. Stefko, *Principal Analyst*, former Senior Research Associate in the government management and economic analysis practices of CGR Inc., a Rochester-based public sector management consulting firm, who holds a doctoral degree with urban policy specialization;

  Robert M. Tocker, M.A., *Associate Analyst*, former Senate Finance and Fiscal Studies Fellow and legislative analyst with the New York State Senate Finance Committee; and

  Heidi Santos, *Administrative Assistant.*

- Rented space through the Buffalo Economic Renaissance Corporation, to circulate funds back for City economic development.

- Adopted and managed BFSA's first budget of under $1 million.

- Adopted procedures relating to Records Access and investments.

Debt Issuance on Behalf of the City of Buffalo

The State legislation that created the Buffalo Fiscal Stability Authority established a framework for BFSA debt issuance on behalf of the City of Buffalo. The financing framework empowers the Authority to borrow to (i) close budget gaps through fiscal year 2007 providing the City and covered organizations implement recurring gap closing actions of their own; (ii) refinance outstanding debt at more advantageous rates; and (iii) incur, as necessary, additional short- and long-term debt on the City's behalf at more advantageous rates than the City itself could achieve.

The Authority's strong financing mechanism results from the structure established by the BFSA Act. All State aid to the City, and all sales tax revenues to the City and Buffalo Public Schools, now flows first to BFSA to back the Authority's bond and note issues and enable high credit ratings on BFSA debt. Debt is issued by BFSA at the request of the City, as proposed by the Mayor or Board of Education and approved by the Common Council.

BFSA's major debt-related action in 2003-04 involved the issuance of $25,745,000 in Sales Tax and State Aid Secured Bonds, Series 2004A, to fund City operating expenses in fiscal years 2004 and 2005. The bond proceeds allow the City to close budget gaps of $7,811,000 in FY 2004 and $19,045,000 in FY 2005. [Note: The $25,745,000 represents the par value of the bonds. As they were issued in the form of premium bonds, total proceeds amounted to $27,783,045 – of which $26,856,000 was used to cover the City's 2003-04 and 2004-05 budget gaps, and the remainder to underwrite issuance costs, BFSA's initial rating, and the cost of preparing revisions to the BFSA Act.] The bonds were sold at ratings of Aa3 by Moody's and AA- by Fitch, insured to the highest Moody's, Fitch and S&P ratings. The underwriter for the Series 2004A Bonds was Lehman Brothers Inc.

BFSA approved short-term cash flow borrowing by the City for $120 million in the form of Revenue Anticipation Notes 2003/2004A in September 2003. [Note: BFSA sold $84 million in Bond Anticipation Notes, Series 2004A-1, in September 2004 to cover cash flow borrowings for 2004-05. The BAN sale was a cooperative effort between the City and BFSA. It received the highest ratings from Moody's (MIG 1) and Fitch (F1+), and did not require letter of credit support, which added approximately $800,000 to the City's 2003 cash flow borrowing.]

Administrative Matters

The Authority hired six employees in 2003 to run day-to-day operations and carry out responsibilities as prescribed by the BFSA Act. As a newly created Authority, BFSA also set up technical and financial management and reporting systems, developed an employee benefit program, adopted investment guidelines, and established administrative procedures. BFSA secured leased office space in a City-owned building in order to defray the costs of its own operations and financings.

Beyond Fiscal 2004

Much was achieved in the first year of the Buffalo Fiscal Stability Authority. The City and covered organizations, in conjunction with BFSA, developed Financial Plans that seek to close structural budget gaps through the implementation of actions that produce recurring savings. Tracking mechanisms were put in place to ensure the City, its agencies and the Authority can effectively monitor budgetary performance during the fiscal year. Financing mechanisms were established to allow the City an opportunity to incrementally close its budget gaps while implementing long-term cost savings. And BFSA established the reporting standards and formats the City and its agencies will employ in the coming years to regularly monitor their fiscal health.

A significant amount of work remains, however. The City and the School District face growing baseline budget gaps in the next four-year Financial Plan. The aggregate combined four-year gap totals $496 million for the City and District. A number of pressing issues need to be addressed:

- **Open labor contracts** with nearly every union in the City and School District represent an opportunity to address major cost centers and bring personnel-related expenses in line with affordable levels. Workforce costs represent three quarters of the City and covered organizations costs. In order to preserve essential services and save as many necessary jobs as possible within the City and covered organizations, it is vital to reform obsolete contracts by reducing costs, not just leveling them.

- **Health insurance costs** continue to rise rapidly without cost sharing by employees. Further, School District unions have not agreed to a single insurance carrier, which would create substantial savings.

- **Obsolete contract provisions** continue to waste significant sums of money, including “no layoff” provisions, unnecessary retirement bonuses and maintenance arrangements that are not bid competitively.

- **Fund balances** are precariously low in the City and School District, providing little cushion against unanticipated budget shocks.

- **Management controls** are lacking throughout the system, hindering the implementation of reforms and cost containment, and in some cases driving up expenditures such as overtime. They must be improved.

- **Additional sales tax sharing** is assumed into both the City and School District Plans in subsequent fiscal years. The City assumes $7 million in 2005-06, $14 million in 2006-07 and $21 million in 2007-08. The School District assumes $6 million in 2006-07 and $9 million in 2007-08. The District also assumes $7 million in additional formula aid beginning in 2005-06 (growing to $11 million in 2007-08) and $12 million in funds related to the Campaign for Fiscal Equity in 2005-06. All of this revenue is highly speculative. Without agreement with Erie County and New York State, both will have to modify their Financial Plans to identify other revenues or cuts in expenditures.

- **Restructuring of the Fire Department** has dramatically slowed. To spearhead this effort, the City must move aggressively to conclude its search for a permanent Fire Commissioner. The department needs a “change agent” who can institute the necessary structural and operational changes.

These and other major problems must be addressed in the coming year. At the same time, BFSA continues to be concerned about the impact of several State statutory mandates within which the City must operate. While the City has some control over the size of its workforce, pension cost requirements are expected to remain high. The burden of pension costs on the City is dramatic, and its increase wipes out much of the personnel savings achieved in BFSA’s first year. Further, the City is saddled with many obsolete contractual provisions (some more than 100 years old) that are no longer affordable or beneficial to taxpayers. These include:

- retirement bonuses;
- “no layoff” clauses;
- no-bid maintenance contracts;
- multiple health insurance providers for School District workers;
- a lack of employee contribution to health insurance costs; and
- a lack of Medicare participation by retirees.

The current system offers municipal workers protections and guarantees that far exceed what the typical private sector worker in the Buffalo community is entitled to:

- health insurance coverage with little or no employee or retiree contribution, despite dramatically escalating costs;
- rich pension benefits with little or no contribution required of the employee;
- in some cases, an ability to retire after twenty years on the job;
- significant job guarantees, reinforced by a system that weakens managerial prerogative to implement cost-saving or efficiency-enhancing reforms; and
- a history of generous wage and benefit increases (until the imposition of the wage freeze in December 2003).

State law has weakened the ability of Buffalo to effectively control local costs. Local officials developed a balanced Financial Plan in order to address the City's solvency under current State-mandated limitations. Nonetheless, the Financial Plan of the City and School District includes a growing amount of speculative assumptions in the out-years. BFSA does not have the power to void contracts or portions thereof. State action is essential to remove major constraints to City reengineering and restructuring. In particular, BFSA has noted that the following laws significantly impede long-term structural balance in the City: the Taylor Law (which establishes impasse negotiation procedures including binding arbitration); the Triborough Amendment (which continues the terms of expired contracts indefinitely); and the Wicks Law (which increases the cost of City building projects, like the new firehouses).

These provide generous (and for the City of Buffalo, unaffordable) protections to municipal workers that raise costs beyond local control and hinder negotiations that might otherwise lead to changes in excessively expensive and inefficient contract provisions. Since labor-related costs represent more than three quarters of all spending – and the cost of the average City employee has risen 8 percent, or $5,366 from 2003-04 to 2004-05 – these reforms are essential to long-term management control and fiscal stability without a continued reliance on increasing amounts of State aid or local tax and fee increases.

A continued collaborative approach to addressing the City's budgetary issues is essential for long-term fiscal stability.

While the City and its covered organizations made progress in BFSA's first year, considerable work clearly remains. Only through strict fiscal discipline and sustained progress toward implementing the gap closing measures in the Financial Plan can these proposals contribute to the City's fiscal health. A continued collaborative approach to addressing the City's budgetary issues is essential for long-term fiscal stability.