

ATTACHMENT #1 – DETAILED ASSUMPTIONS

As noted in the Executive Summary, financial forecasting includes numerous assumptions and components that can fluctuate based on a variety of actions. The budgetary projections for 2019 through 2021 presented by staff in this agenda item utilize numerous assumptions outlined in detail in this document. These assumptions are based on current policy decisions, current economic conditions, known expense and revenue variables, and projected actions; however, it is critical to understand that changes to any of these documented assumptions (or others) will have an impact on future annual budgets presented to the City Council.

Prior Assumptions/Financial Principles

In 2015, the City implemented three financial principles that guide financial decisions. These principles were developed to promote the long-term financial success of the community. The following principles were adopted:

- *Principle #1* - The City will pass a structurally balanced operating budget annually;
- *Principle #2* - The City commits to continuous improvement in the delivery of necessary and cost-effective services; and
- *Principle #3* - The City will actively seek to increase its reserves to 25% and reduce its debt by 25% in the next eight years.

When the City instituted these principles, they were based on several assumptions being fully realized. These are outlined in the chart below.

MAJOR ASSUMPTIONS		DID IT HAPPEN?
Limiting the increase in the operating budget to no more than 3% annually		Yes
Planning moderate pension growth		No
Expecting \$16 to \$17 million of capital with undedicated revenue sources		Yes
Projecting conservatively for future revenues		Yes
Holding operating expenses in line with planned revenues		Yes
Aligning fees and charges appropriately with the total cost of service		Yes
Maintaining a flat property tax rate		No
Utilizing the home rule sales tax for debt reduction and future borrowing		Yes
Unchanging actions at the state level		No
Utilizing revenue from sale of assets to offset capital or reduce debt		Yes
Evaluating future revenue against four criteria		Yes
Minimizing risk for our AAA bond rating		Yes

Unrealized Assumptions

As noted above, three major assumptions utilized in 2015 during the development of the financial principles have not been realized, resulting in changes to budgets and future budgetary projections. Below is a brief synopsis of the impact of those assumptions not being realized.

1. Pension Growth

Since Fiscal Year (FY) 2007, the City has experienced a 144% increase in required pension payments. Additionally, the City saw a 16% increase from CY17 to CY18 alone, placing significant pressure on the City's annual budget. The recent increases have been caused by several factors that included, but are not limited to, changes in the mortality tables, payroll growth and fluctuations in market returns on the pension investments. In addition, the City's current pension funding methodology requires 100% funding by 2033, compared to the state's minimum requirement of 90% by 2040. Overall, the City's pension funding practices have led the City to have the highest funding percentage level of comparable public safety pensions, with a combined funding ratio of 72.3%, which is the actuarial value of assets versus actuarial accrued liabilities.

	FY07	CY17	FY07 to CY17 Increase	CY18 Budget	Annual Increase
Police Pension	2,762,370	6,538,474	137%	7,129,194	9%
Fire Pension	2,883,432	7,237,440	151%	8,896,264	23%
Public Safety	5,645,802	13,775,914	144%	16,025,458	16%

2. State Pressures

As part of the State of Illinois' budget compromise in 2017, several items were introduced that impact Naperville's financial picture in 2018 and beyond. Specifically, two items reduce the overall revenue received by the City from the state:

- *Sales Tax Administrative Fee* - The state implemented a 2% administrative fee on the collection of the City's home rule sales tax. Based upon current home rule sales tax receipts, this administrative fee is projected to reduce revenue by \$175,000 for a 0.50% home rule sales tax rate.
- *State Income Tax* - The state reduced the municipal allotment of state income tax through the Local Government Distributive Fund (LGDF) by 10% through June 2018. This reduced the City's budgeted revenues in 2018 by \$750,000. As part of the Governor's 2018 budget proposal, the reduction of LGDF is being extended. This will reduce the 2018 budget by an additional \$650,000, for a total reduction of \$1.4 million. Staff is projecting that these reductions will continue in 2019 and beyond.

3. Property Tax Policy Decision

The City's property tax levy includes several components, including City operations, public safety pensions, debt service, Naper Settlement and the Naperville Public Library.

A property tax abatement was implemented as part of the approval for the home rule sales tax in 2015. Set at \$2 million, the abatement reduced the City's property tax levy from \$48.4 million in 2015 to \$46.4 million in 2016. Combined with that year's equalized assessed valuation (EAV) growth, the property tax rate decreased from 0.8081 to 0.7392. Per the assumptions utilized when setting the City's three financial principles, this

abatement was anticipated to expire in 2017 and the property tax rate was estimated to return to the original 2015 rate of 0.8081. In 2017, City Council made the policy decision to keep the property tax levy flat at \$46.8 million. Combined with the impact of that year's EAV growth, the property tax rate again decreased from 0.7392 to 0.7004.

The policy decision by the City Council to maintain a flat property tax levy versus a flat property tax rate has reduced the amount of property taxes received by the City over the past two years. Maintaining the property tax rate at the same level would have allowed the City to take advantage of incremental EAV growth, including new development. If the City had maintained a flat property tax rate versus a flat property tax levy, an estimated additional \$9.15 million of revenues would have been received from 2016 to 2018.

	EAV Valuation	Actual Rate	Extension	Flat Rate	Extension	Difference
CY15	5,993	0.8081	48.43	0.8081	48.43	-
CY16	6,279	0.7392	46.41	0.8081	50.74	4.32
CY17	6,668	0.7004	46.70	0.8081	53.88	7.18
CY18 (Projected)*	6,934	0.6762	46.89	0.8081	56.04	9.15

**4% EAV Growth and Holding Extension Flat
in Millions*

Current Assumptions/Financial Projections in 2019-2021

As noted in the previous section, changes to assumptions utilized in creating the City's annual budgets results in a ripple effect that impacts the forecasts for future budgets. In creating the 2019-2021 budget projections, staff utilized current policies and current economic conditions, along with relevant historical data, to craft the projections outlined in detail in Attachments #2 through 6.

General Methodology/Overall Assumptions

Average Annual Increase

- *Expenditures*
 - 3-year average change for expenditures
 - Consistent with existing collective bargaining agreements
 - Consistent with current operational practices and services provided
 - Consistent with existing contracts and agreements
 - Minimizes inflationary impact
- *Revenues*
 - Usage of both short-term and long-term trends
 - Hold constant for any changes in revenues
 - Includes change in state methodologies
 - Includes changes in local rates

Upper and Lower Bounds

- 10 years of data, adjusted for inflation
- Minimizes annual fluctuations due to weather or other one-time events

- 95% confidence interval

Risks and Opportunities

- Household Hazardous Waste Facility (HHW)
 - Potential for increased costs of disposal of hazardous materials and insurance requirements for hazardous materials per review of existing State of Illinois agreement
- Legal Settlements
 - Outstanding legal claims against the City
- State Actions – Property Taxes
 - Additional unfunded mandates, further reductions in shared revenues or implementation of a property tax freeze
- Administrative Hearing Process
 - Review of moving hearings to a City site with the potential to increase revenues for the City
- Service Fee Reviews
 - Continued annual review to align service delivery costs with fees for service
- Downtown Streetscape Project
 - Currently not included in the 5-year Capital Improvement Program; including this would increase annual capital requirements
- Ogden Avenue Corridor Enhancement Project
 - Full scope and value of project is not currently included in the 5-year Capital Improvement Program. Including this would increase annual capital requirements
- Fire Station Consolidation
 - Review of service levels and coverage areas associated with Fire Stations #5 and #6
- 5th Avenue Project
- Parking Decks
 - Potential for the reconstruction and/or rehabilitation of the Chicago Avenue Deck
 - Potential for increased costs of maintaining the Van Buren Parking Facility

Expenditures Assumptions

Overall Assumptions

- Average annual spending increase of 0.3% across all funds and expense categories
- Upper and lower bounds are set at a confidence interval of 1.8%, meaning that overall expenditures have a risk of being 1.8% higher than projections or potential of being 1.8% lower than projections

Salaries and Wages

Regular Pay

- Maintains existing headcount figure of 948.36 FTEs; this includes full-time, part-time and temporary employees
- Headcount figures for Naper Settlement and Library remain consistent

- Uses existing collective bargaining agreements for agreed years for union employees
- Uses weighted average of collective bargaining agreement for non-union and out-of-contract employees. 2.09% in Year 1; 2.22% in Year 2; and 2.00% in Year 3
- Historical 1.0% annual increase

Overtime

- Grows at rate of wage increase
- Historical 1.0% annual increase

Other Salaries and Benefits

- Includes Temporary Pay, other compensation, vacancy factor
- Grows at rate of wage increase
- Excludes Special Census workers starting in 2019

Benefits and Related

Payroll Benefits

- Includes Social Security and Medicare
- Grows at rate of wage increase

IMRF

- Historical 0.5% annual decrease
- Historic rates from IMRF:
 - 2018 = 11.12%
 - 2017 = 11.37%
 - 2016 = 11.78%
 - 2015 = 11.61%
 - 2014 = 12.36%

Healthcare Benefits

- Historical 8.4% annual increase
 - Premiums, claims, and administrative fee
 - Savings due to Prescription Drug Program
 - Change in benefit package design
 - Decrease in employees covered
 - Change in retiree healthcare program – Medicare supplement program

Other Insurance

- Includes boiler insurance, auto liability; worker's compensation; property insurance; surety bonds; settlements and general liability
- Historical 12% annual increase

Pensions

- Utilization of Foster and Foster modeling tool
 - 15-year rolling average – open methodology
 - Entry age normal

- 7.0% annual earnings
- RP2000 mortality tables with annual adjustments
- 100% funding level by 2033
- Use of Food and Beverage Tax receipts to fulfill pension obligations not additional
 - Projected 4.5% annual growth in Food & Beverage Tax receipts

Purchased Services

Refuse and Recycling Contract

- Significant increase projected in 2019 as contract expires; same recycling price of \$2.43/per household per month has been in place since early 1990s
- Continuation of existing service provision
- Continuation of existing pricing methodology
 - Currently set services and ask-for price versus the potential to set price ask for services
- Continuation of service fee pass-through to residents via utility bills
- 10% projected increase for 2019 with 2% CPI adjustment in 2020 and 2021

Credit Card Fees

- Uses a 4-year history since expenditure has been itemized
 - Historical 18% annual increase
- Assumes no implementation of credit card surcharge fee
 - If charge is implemented, usage may drop off
 - Card companies responsible for pursuing payment on delinquent accounts; if card usage drops, collections costs increase as collections is the method used for delinquent accounts on other payment methods

Technology

- Ramp-up of technology and software over last two years with implementation of ERP and planned usage of Cityworks and additional support services for technology and hardware purchases
- Historical 6.0% annual increase
 - Utilized support services and technology as historical reference points

Repair Services

- Building and Ground Maintenance – 4.5% annual increase
 - As buildings continue to age, maintenance costs increase
- Equipment Maintenance – 4.0% annual increase
 - Primarily due to aging fleet and continued increase in contracted services

All Other Purchased Services

- Historical 0.7% annual increase
 - Primarily due to seasonally dependent services and expenses such as winter operations, brush collection and leaf collection

Purchased Items

Major Commodities/Utilities

- Purchased Water
 - Average use of 5.38 billion gallons (10-year average consumption) and 1% price increase by DWC
 - Direct pass through to consumer
- Purchased Electricity
 - Annual 1.5% increase per IMEA projections
 - Adjusted through usage of Purchased Power Adjustment (PPA)
- Fuel and Oils
 - Consistent gallonage usage and consistent pricing based upon current trends; susceptible to volatile pricing
- Salt and other chemicals
 - Year 1
 - Increasing tonnage from 10,500 to 14,000 tons to replenish domes after heavy winter
 - Increasing price from \$45/ton to around \$51/ton based upon historical trends
 - Year 2 and 3
 - Stabilize tonnage and increase price 5% based upon historic trends

Cost of Utilities for City Facilities

- Electric Expense – Projected 2.4% annual increase
 - Based upon consumption and utility rate study
- Water Expense – Projected at 4.1%, 3.1%, 1.8% annually
 - Based upon consumption and utility rate study
- Natural Gas Expense – Projected flat
 - Based upon consumption and historical/current market prices
- Internet and Telephone - 2% annual increase

Non-Itemized Purchased Services

- Historical 1.6% annual decrease

Debt Service

- Utilizes current debt service schedule
- Adds an additional \$7.25 million in annual borrowing
 - Maximum amount that can be borrowed annually to align with principle #3
- No additional borrowing for enterprise or special funds, including special service areas
- Borrowing parameters
 - 3.5% interest rate
 - 20 year loan
 - Payoff 20% of principal and interest in first 5 years
 - Payoff 50% of principal and interest in first 10 years

Interfund Charges

- Re-Payment of Water loan from Electric Utility based upon current schedule
 - Ends in 2020

- Insurance Interfund Transfers
 - Includes boiler insurance; auto liability; worker's compensation; property insurance; surety bonds; settlements and general liability
 - Historical 12% annual increase
- Debt Service Transfers
 - Utilized for paying of General Obligation Debt, offset to property taxes
 - Food & Beverage – Based upon F&B allocations in current ordinance
 - SSA #21 – Consistent based upon prior year transfers
 - Water Street TIF – Consistent based upon prior year transfers
- IT Service Transfers
 - Based upon IT service costs; growth projected at 6.0% commensurate
- E-911 Transfers
 - Funds will match revenues received – 5% annual increase projected
- SSA #26 Transfer
 - City's two-thirds split for maintenance expenses in the downtown
 - Historical drawdown of fund balances has alleviated property taxes and transfer from General Fund
 - Projecting a 20%, (approximately \$200K) increase for year 1 and 2% in Year 2 and 3

Capital Outlay

- Based upon current 5-year Capital Improvement Program
 - 2019 = \$79.40 million
 - 2020 = \$79.54 million
 - 2021 = \$55.66 million
- Includes all funding sources, including reserves, developer contributions, other governmental contributions, taxes, and unfunded projects
- Fund Overview
 - Bond Fund – Cap of \$7.25 million for borrowing
 - Capital Projects Fund – Includes increased HRST, private contributions, other governmental contributions
 - Electric Utility Fund – \$12 million annually based upon rate study
 - Water Utility Fund – Based upon rate study and includes preliminary phosphorus work
 - Maintenance Improvement Program – Includes ramp-up from current \$10 million investment to \$12 million investment over 4 years
 - Other Funds – Includes Library, Settlement, Downtown and Commuter Parking; estimates based upon 5-year CIP

Contributions to Other Entities

- Historical 2.8% annual increase
- Grants
 - Social Service Grants – Consistent at \$500,000 from Food and Beverage
 - SECA Grants – Increase 2% based upon February 26 Council SECA Workshop recommendations
 - PACE Ride Share, Ride DuPage – 2% annual increase

- Community Development Block Grants – 2% annual increase
- Cost Sharing Agreements
 - Naperville Park District – Carillon and Riverwalk Maintenance – 2% annual increases
 - NCTV - Funding from PEG fees and supplemental General Fund Expenses – 2 % annual increases
 - Naperville Development Partnership – Portion from Hotel/Motel Taxes; Electric and Water Utilities – 2% annual increases
- Pass Throughs
 - ETSB Fund – Direct funds to Aurora for their ETSB
 - Funds will match revenues received – 5% annual increase

Revenue Assumptions

Overall Assumptions

- Average annual revenue decrease of 2.0% across all funds and revenue categories
- Upper and lower bounds are set at a confidence interval of 2.7%, meaning that overall revenues have the potential of being 2.7% higher than projections or the risk of being 2.7% lower than projections

Property Taxes

- Components of Standard Property Tax Bill
 - General Corporate
 - Amount determined by difference in projected annual operating expenditures and revenues
 - Is used to align with Financial Principle #1
 - Debt Service
 - Utilizes current debt service schedule
 - Adds an additional \$7.25 million in annual borrowing
 - Max amount that can be borrowed to align with Principle #3
 - Use of debt service transfers from Food & Beverage, SSA #21 and Water Street TIF to offset property taxes and payoff General Obligation debt
 - Pensions
 - IMRF – Based upon cost projections - Historical 0.5% annual decrease
 - Public Safety Pension
 - Utilization of Foster and Foster modeling tool
 - Continued use of Food and Beverage receipts to fulfill pension obligations not in addition to the required contribution
 - Naperville Public Library
 - Projecting a 4% increase for year 1 and 2% in years 2 and 3
 - Historical drawdown of fund balances has alleviated property taxes
 - Increase required for structurally balanced budget
 - Naper Settlement
 - Projecting a 8% increase for year 1 and 4% in years 2 and 3

- Historical drawdown of fund balances has alleviated property taxes
 - Increase required for structurally balanced budget
 - Includes an increase of annual Heritage Society contribution from \$615K to \$650K to offset a portion of the annual property tax request
- Special Service Areas
 - SSA #21 – No change projected for repayment of Van Buren Parking Deck
 - SSA #23 – Slight increase projected in 2019 based upon sales tax rebate agreement; revenues are transferred to debt service fund
 - SSA #25 – No change projected for repayment of traffic signal
 - SSA #26 – Projecting a 20% increase for year 1 and 2% in years 2 and 3
 - Covers 100% of marketing expenses and one-third of downtown maintenance expenses
 - Historical drawdown of fund balances has alleviated property taxes and transfer from General Fund

Sales Taxes

- State Sales Tax
 - 1.4% annual growth Projected; includes rebate agreements
 - Review of both long-term and short-term trends
- Home Rule Sales Tax
 - Increase from 0.50% to 0.75%
 - 4% annual growth projected
 - Continuation of 2% administrative fee from State of Illinois
 - Continue to make downtown parking fund whole
 - Continue to use HRST for debt service and capital projects
 - Incremental \$4.4 million in 2018 used for reducing capital borrowing

Locally Administered Taxes

- Hotel & Motel Tax
 - Increase of Rate from 4.4% to 5.5%
 - Receipts projected to increase by 25% in 2019 and 2% thereafter
 - Includes increase in rebate agreements
- Food & Beverage Tax
 - Annual increase of 4.5%
 - Grows consistently; downward economic pressures have minimal impact
 - Distributions based upon allocations in current ordinance for social services, SECA grants, pensions and debt service
- Local Gasoline Tax
 - Projected 1% annual decrease in receipts; similar trend to motor fuel tax
 - Overall gallonage has decreased slightly
 - Any shortfall of local gas tax from projections would have to be covered by HRST or capital deferrals if the MIP is to be funded at the current levels
- Real Estate Transfer Tax
 - Projected 4.8% annual growth; reviewed 10 years for growth factor
 - Highly variable tax based upon market conditions

State and Local Shared Taxes

- State Income Tax
 - Continued 10% reduction of LGDF
 - Projected annual cost of \$1.4 million
 - Incremental increase starting in 2019 from Special Census results
 - 3% addition – approximately 4,500 new residents projected
- Motor Fuel Tax
 - Projected 1.5% annual decrease in receipts; similar trend to local gas tax
 - Overall gallonage in state has decreased slightly
 - Potential for slight increase after completion of Special Census
 - Any shortfall of local gas tax from projections would have to be covered by HRST or capital deferrals if the MIP is to be funded at the current levels
- Personal Property Replacement Tax
 - 0.9% annual decrease projected; based on short-term trends
- Local Use Tax
 - Projected 1.5% annual increase
 - Potential for higher increase after completion of Special Census
- Auto Rental Tax
 - Projected 1.3% annual increase
- E911 Surcharge
 - Projected 5.0% annual increase
 - State has changed distribution for E-911 surcharges in last 2 years
 - Aurora joined the City's ETSB in December 2017
 - Revenues received for Naperville continue to be a pass through to the General Fund and revenues received for Aurora are a direct pass through
- Local Share of Township Road & Bridge Fund
 - Portion of the township property tax levy
 - Projected 5% annual decrease based on 3-year trend

Utility Taxes

- Electric Utility and Water Utility Taxes
 - Match the increases in the Water Utility and Electric Utility rate studies
 - Based upon consumption and price
- Natural Gas Tax
 - 10% annual decrease projected
 - Last two years have been mild winters with depressed usage
 - Natural gas prices have declined over last 10 years
- Telecommunications Tax
 - 5% annual decrease projected
 - Increased rate from 5% to 6% in CY2018

Charges for Service

- Electric Utility Charges
 - Overall 2.4% annual increase all 3 years based upon 2016 rate study
 - Currently starting new rate study; figures will be updated

- Water Utility Charges
 - Rate increases based upon 2017 rate study
 - Goals of rate study included building cash reserves for phosphorus improvements, increasing capital funding for infrastructure, re-building 30-day cash reserves and developing structurally balanced budget
- Refuse Collection Charge
 - Significant increase projected in 2019 as contract expires; same recycling price of \$2.43 per household per month has been in place since early 1990s
 - Continuation of existing service provision
 - Continuation of existing pricing methodology;
 - Currently set services and ask-for price versus potential to set price and ask for services
 - Potential to set price and ask-for services
 - Continuation of service fee pass-through to residents via utility bills
 - 10% projected increase for 2019 with 2% CPI adjustment in 2020 and 2021
- Ambulance Billing Fees
 - 4.8% annual growth projected
 - Analyzed 7 years prior to implementation of increased fee to determine annual growth rate
- Department Service Charges
 - Increases at rate of personnel costs
- Library and Naper Settlement Charges
 - Flat projection for rentals, tours, programming and other charges
- Other Billable Services
 - Includes damage recovery, fire alarm monitoring, administrative tow fees and resale items
 - Flat growth assumptions

Development Related Revenues

- Includes licensing, building permits, permit fees, inspections and review fees
 - 5.9% annual growth projected
 - Assumes current trend of consistent development and growth

Grants and Intergovernmental Agreements (IGA)

- Flat assumption for all grants and IGAs
- Assumes continuation of the following major grants and IGAs
 - Community Development Block Grant (CDBG)
 - Household Hazardous Waste Facility
 - State Per Capita Grant (Library)
 - Naperville Fire Protection District
 - Service Agreements with State and Counties – mowing, traffic signals

Fines, Fees, and Surcharges

- Service Fees
 - Includes service fees, late payment fees, turn-on fees, installation fees and other fines

- Flat growth assumptions
- Parking Permits
 - No change to rate; projected flat over 3 years
- Parking Fines and Ordinance Violations
 - Flat growth assumptions
- Traffic Fines
 - \$1 million annual assumption starts in 2019; down from \$1.2 million in 2018
 - Sharp decline from peak of receipts of \$2.9 million in 2010; have seen a leveling from the annual decrease over last 2 years

Interfund Transfers

- Re-payment of Water Loan from Electric Utility through 2020
- Debt Service Transfers – Offset to property taxes
 - Food & Beverage – Based upon F&B allocations in current ordinance
 - SSA #21 – Consistent based upon prior year transfers
 - Water Street TIF – Consistent based upon prior year transfers
- Service Transfers
 - Includes IT and Fleet services; consistent with projected growth in expenses
- SSA #26 Transfer
 - Continuation of existing Special Service Area – Expires in 2020
 - City's two-thirds split for maintenance expenses in the downtown
 - Historical drawdown of fund balances have alleviated property taxes and transfer from General Fund
 - Projecting a 20% increase for year 1 and 2% in years 2 and 3

Other Revenues

- Bond Sale Proceeds
 - To align with Principle #3 the maximum available to borrow on an annual basis is \$7.25 million
- Insurance Premiums and Benefit Transfers
 - Increase of 8.4% commensurate with projected insurance cost increases
- Interest & Investment Income
 - 2% projected growth; stabilized cash after drawdown over last 10 years
- Franchise and PEG Fees
 - Related to AT&T, Comcast and Wide Open West
 - 1.2% annual decrease projected based upon 10-year historical trends
- Other Receipts
 - Flat growth assumptions
 - Includes rental income, bad debt, rebates, sale of property, etc.
 - Rental income
- Contributions
 - Capital contributions
 - Based upon 5-year Capital Improvement Program
 - Includes developer and other governmental contributions for projects