



Fairbanks North Star Borough

Office of the Mayor

809 Pioneer Road

P.O. Box 71267

Fairbanks, Alaska 99707-1267

907/459-1300

Fax 907/459-1102

Email mayor@co.fairbanks.ak.us

May 15, 2008

The Honorable Nadine Winters
Presiding Officer
Fairbanks North Star Borough Assembly

Dear Ms. Winters:

This budget must be responsive to the reality of changing economic circumstances throughout the Fairbanks North Star Borough. The budget must also continue to be consistent with sound budgetary principles; specifically:

- The Borough will provide those services and facilities which a majority of the public demands.
- The public must then be willing to pay for that which it demands.
- The delivery of Borough provided services and the condition of Borough provided facilities must be maintained to a standard of excellence.
- Efficiency is required.
- Economic growth must be a significant budgetary goal.
- Public trust must be maintained throughout the budget process including both the revenue and expense components.

The budget adheres to these principles and will accomplish these goals. A narrative has been provided in past budget messages regarding the considerations listed above. The remainder of this message will focus on the changing economic reality we are tasked to deal with.

The underpinning of the Fairbanks North Star Borough economy is changing; the cost of energy has risen to an unprecedented level at an unprecedented rate of increase (see attachment A and B). The outcome of this paradigm shift is yet to be clearly

understood. What is clear is that the significant run-up for the cost of energy from existing sources to our community is not a short term anomaly. It is probably a long term reality, and the Borough as a government entity and all citizens, as a community, must be responsive.

The budget as presented is the initial budgetary response from the Borough government. The response has several guiding principles:

1. Recognition that change exists, and can not be ignored.
2. Recognition that over reaction can be harmful, and therefore response should be incremental, monitored and deliberative.
3. Recognition that the Borough government has a leadership responsibility, not only manifested through budgetary restraint but also by providing funding for specific energy solution implementation.

The Borough's leadership responsibility also transcends the budget. The entire community must be engaged and informed of the magnitude of the change and definitive options for dealing with it, as those options become available.

During the last three and a half years, the base-line cost of energy across the Borough has more than doubled; from around \$200M per year, to around \$450M per year. Wage growth has lagged behind this significant increase in the direct and required cost of living here; therefore, the net result is a significant reduction (if not elimination for many families and individuals) of discretionary income. This conclusion is especially pointed in the case of the FNSB because the overwhelming percentage of this increase in cost migrates directly out of the community and does not re-circulate. The net effect to the Borough economy is roughly equivalent to the direct cost of the closure of Eielson Air Force Base.

* The base-line does **not** include refinery internal use, UAF, aviation or military useage/cost.

The budget as presented responds to this circumstance in a measurable manner:

- The general fund budget has decreased \$1,323,040.
- Taxes paid by existing Borough taxpayers have decreased by \$3,966,722; excepting TAPS.
- Taxes levied are \$6,940,851 under the allowed tax cap.
- The areawide tax mil levy is 11.287 the lowest rate in 20 years.
- The budget utilizes funds set aside for future tax relief of \$3,773,030.

Additionally, the budget honors all contractual obligations of the Borough and provides for anticipated cost increases. In short, the budget is responsive to our changing circumstance, responsible and mindful that over reaction can be harmful.

In alignment with the final guiding principle, the Borough also has a responsibility to ensure that specific energy solution components are implemented and paid for. In March of this year, the Fairbanks Economic Development Corporation (FEDC) received responses to a request for proposals for an energy delivery system based on coal/bio-mass conversion. The intent is that the community will be provided an opportunity to review energy options that utilize existing commercial technology at known costs and known benefits. FEDC receives significant funding from the Borough. Additionally, the Borough is currently circulating a request for proposals which will provide for consideration of a municipal waste to energy option; this effort is funded through the operating budget. Further, the Borough continues to exercise all possible pressure and influence to expedite a natural gas pipeline; in part, this effort is pursued by the Alaska Gasline Port Authority, of which the Borough is a member and to which the Borough is a financial contributor. Also, the Borough is collaborating with Aurora Energy to determine costs and benefits for substantial expansion of the existing district heating system; it is anticipated that Borough funding for this effort will come from economic development funds. Also, the budget provides for funding a Borough-wide energy manager, tasked with analysis and then recommending cost effective energy conservation measures; firstly, at Borough facilities and secondly, throughout the community. The Borough is also working closely with a number of public and private

Letter to the Honorable Nadine Winters

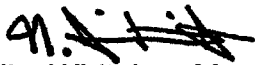
May 15, 2008

Page 4

entities including: Chena Power/United Technologies, Usibelli Coal Mine, Wachovia Securities, Fairbanks Economic Development Corporation, Interior Regional Housing Authority, Cold Climate Housing Research Center, University of Alaska Fairbanks, Alaska Housing Finance Corporation, Golden Valley Electric Association, Alaska Energy Authority, U. S. Department of Energy, the Governor, the Legislature, the Alaska Congressional Delegation and others. The intention of these specific efforts and collaborations is to fulfill the Borough's obligation to deal with the energy crisis we are facing, in a manner which leverages Borough funds, is credible and has the most probable successful outcome in the least amount of time. More narrowly, the efforts and collaborations are consistent with the Fairbanks Regional Energy Flex Plan; which requires a goal oriented result: to stabilize and reduce energy costs.

The budget is consistent with proven and sound budgetary principles. It also provides for initial specific responses to the upward paradigm shift of energy costs. The budget manifests the reality that our community must compete and invest in whatever arena is necessary in order to provide ourselves a self-determined and prosperous future. We, as a Borough government and we, as a community, have no choice but to boldly move forward.

Sincerely,

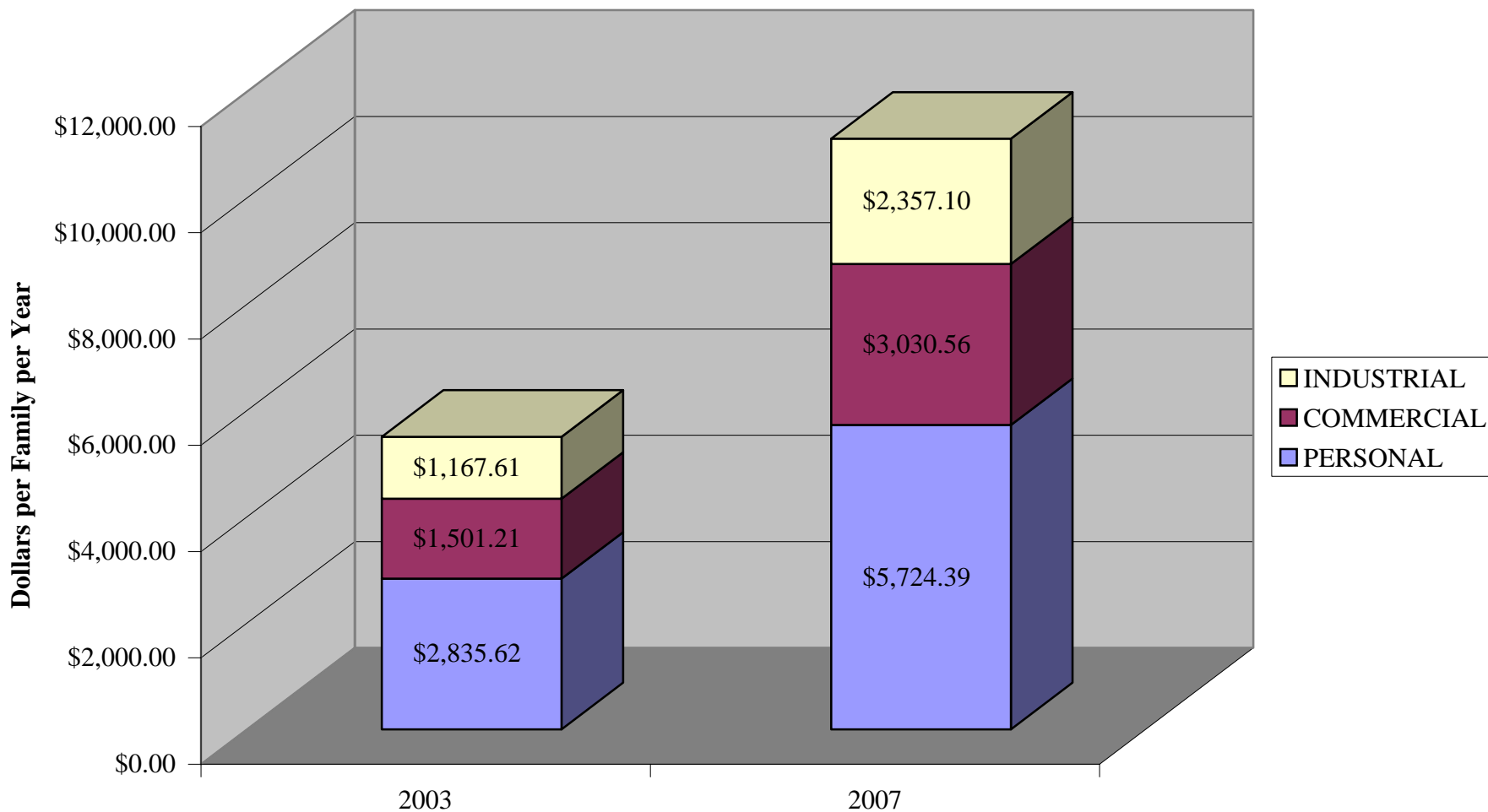


Jim Whitaker, Mayor

JW:csm

Attachments: 2003 & 2007 FNSB Annual Energy Cost Comparison by Household
FNSB Per Capital Energy Cost

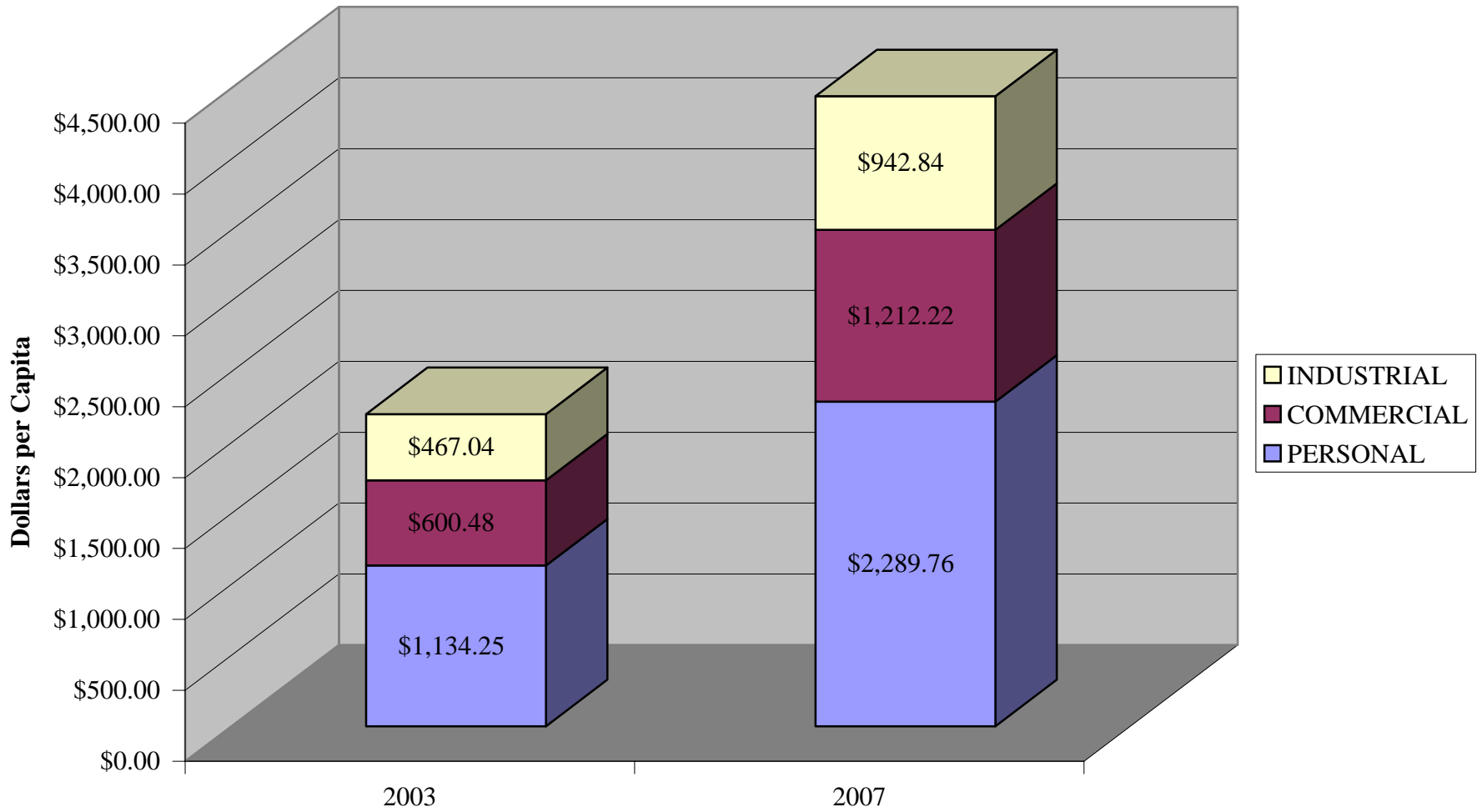
2003 & 2007 FNSB Annual Energy Cost Comparison by Household*



Source: FNSB Community Research Center, FNSB Economic Development , Golden Valley Electric Association, Interior Issues Council Energy Task Force

* Household is assumed to be 2.5 people

FNSB Per Capita Energy Cost



Budget Highlights

Organizational Highlights

NOTEWORTHY BUDGET ACCOMPLISHMENT/CHANGES/ADJUSTMENTS/CONSIDERATIONS

- A significant noteworthy accomplishment of this budget is that, even though the CPI increase used to develop this budget is 2.2%, the average increase in taxes on properties that were on the tax rolls at 12/31/2007 is a negative number. Specifically, \$3,966,722 less in taxes are being collected from those properties on the tax rolls last year, than will be collected this year, excluding TAPS.
- The calendar year (CY) 2008 mill rate is 11.287, or a (.922) decrease from the CY 2007 levy of 12.209. This reduction equates to a 7.55% decrease in the mill rate, making it the lowest rate since 1988. The Non-areawide and the Solid Waste Collection District mill rates have remained basically stable, with slight decreases.
- There is a \$1,104 increase in the overall budget, as compared to a 2.2% CPI. The fiscal year (FY) '08 revised budget of \$126,807,946 increased to \$126,809,050 in the FY '09 approve budget.
- Overall, in terms of dollar size, employee count, and mill rate settings, this is a very tight maintenance level budget.
- To provide taxpayer relief, this budget incorporates and temporarily uses \$3.25M of Facility Maintenance Reserve funds to reduce needed property taxes which the Borough anticipates will be replenished from the projected \$3.86M of Revenue Sharing dollars that it should receive from the State.

MAJOR ISSUES AND CONCERNS

- The PERS and TRS rate uncertainty issue has been (for the foreseeable future) addressed by the Legislature. Legislation forwarded to the Governor's Office requires school districts to only pay the normal cost rate (12.56% for FY '09), with the State paying all past service cost rate components. PERS employers (inclusive of the FNSB) will pay a flat rate of 22% on both their defined benefit and defined contribution employees. This rate has member employers paying a portion of the unfunded liability (approximately 8% of salaries in FY '09). This same legislation changes the law to say that PERS is a consolidated system, the result being that in future years the Borough's financial statements will no longer reflect any unfunded pension obligation.
- Trans Alaska Pipeline System (TAPS) assessed valuations for assessment years 2006, 2007, and 2008 have had objections filed. The ultimate resolution to these filings will take years and the then determined outcome is uncertain. The Borough is required to use the State set valuations in building its budgets, these valuations affect mill rate calculations and actual taxes collected from TAPS. There exists a possibility that the Borough may have to refund taxes in the future, said amount (if any) of course being unknown at this time.
- The Borough Clerk's Office has certified that an Initiative petition submitted on Wednesday, October 9, 2007 will be place before Borough voters at the October 7, 2008 Regular Election. This Initiative, unlike prior years tax cap Initiatives, removes new construction or property improvements from the tax cap calculation. Should this be passed by voters, future revenues to all taxing jurisdictions will be severely and negatively impacted. The delivery of Borough and service area programs and services will be materially impacted and will ultimately have to be curtailed.
- There have been recent efforts to increase the reduction of State education foundation formula dollars to School Districts by the equivalent of 3 mills (versus 2 mills) times the full and true value increases in real and personal property within the Borough, as determined by the State Assessor. Such a change has the potential of an additional reduction in the foundation formula fund given to the School District by the State of up to \$1M a year. Essentially, through a formula, State funding for education is reduced as local property (real and personal) values increase. Formula wise, going from an effective rate of 2 mills to 3 mills equates to a 50% increase in the size of the funding reduction coming from the increased property values. In all likelihood, the District would come to the Borough to make up this funding loss which the Borough will have difficulty managing due to tax cap limitations.
- Maintaining a relationship wherein the real rate of taxation in dollars is less than the per capita income rate of growth in dollars. Maintaining economic growth and new construction trends into future years is critical in this relationship.
- New construction assessed values added to the tax roles have for the last ten years been fairly steady at about 5% per year. These new values help keep the mill level stable for existing property owners, but the 5% average addition of new construction isn't likely sustainable in the long-term.

Budget Highlights

Organizational Highlights (Continued)

- Balancing escalating Borough operation costs, such as energy cost increases, with escalating funding to community interest groups is becoming more of a budget challenge.
- Impacts of the Borough's aging workforce are four-fold: 1) health care cost containment becomes more challenging, 2) as individuals in key management positions approach retirement eligibility, there is concern over a loss of institutional knowledge, 3) hiring "qualified" staff as the overall work force shrinks (boomer effect), and 4) if we find "qualified" staff, the impact of competing wage levels and benefit packages compounds hiring and retention challenges.
- Identification of local revenue alternatives to replace lost State capital matching grant program funds, and the continued increases in State mandated senior citizen and disabled veterans property tax exemptions is needed.
- There is a need to put into place, or find, an adequate annual funding source for the facilities maintenance reserve fund, with the recent non-funding of the capital matching grant program this is a more critical concern.
- The significant negative trends in local energy costs are of concern in terms of the noticeable added operational costs to the Borough, in terms of the overall restraining impact it has on local economic development, in terms of the forced reduction of personal discretionary dollars available to Borough residents, and ultimately on the material net export of liquid financial assets out of the community.
- A period, such as we saw in the early 2000's, of extraordinarily low fixed-income investment returns as a result of the financial markets being under great stress has returned. Events have led the fed-funds rate to be drastically cut in the last several months. Unfortunately, the Borough's fixed-income investments materially track this rate, and accordingly, investment income has come down significantly and will likely stay down for an extended period. The impact over even a short time period will be several millions of lost investment revenue dollars.

Expenditure Highlights

LOCAL EFFORT TOWARD EDUCATION

- 55.7% of general fund revenues are dedicated to education, comprised of the direct local contribution of 42.2% (\$44,222,700), and 13.5% (\$14,167,840) for school debt servicing. In addition to providing all of the school buildings and facilities, there are other additional indirect administrative services provided that equal \$763,400 which are waived by the Borough. Some of these contributions not displayed in the budget include legal services, banking services and cash management, and other services.

LOCAL EFFORT TOWARD MULTI-YEAR PROJECTS

- Due to State funding cuts, the Capital Matching Grant Program provides no funding in this budget.
- The Facilities Maintenance Reserve Fund appropriation decreased from \$2,000,000 to \$0.

LOCAL EFFORT TOWARD DEBT SERVICING

- Total debt servicing decreased \$2,419,870 from FY 2008's \$16,587,710 to FY 2009's \$14,167,840.
- Total existing areawide debt will be \$143,163,000 at June 30, 2008 and \$135,260,000 at June 30, 2009.

LOCAL EFFORT TOWARD GRANTS

- Funding for local grants and to matching grants was \$2,225,339 in FY '08; the FY '09 Budget has \$2,021,500.

WAGE AND BENEFIT ADJUSTMENTS

- The benefit rate is 63.6%, up from FY 2008's 63.4%.
- Union contracts were renegotiated during FY 2006. The new contracts allow for a cost-of-living increase to be added to the pay scales for FY 2007, FY 2008, and FY 2009. The cost of living adjustment for FY 2009 is based on the annual rate of inflation, using the Anchorage CPI Urban. The rate of change is based on calendar year average to calendar year average, and is 2.2% for FY'09.

Budget Highlights

Expenditure Highlights (Continued)

STAFFING CHANGES TO BOROUGH SERVICES AND PROGRAMS

- Borough-wide, benefit eligible employees decreased by four employees from FY 2008's Budget of 413.

<u>SUMMARY OF EMPLOYEE CHANGES</u>	
FY 2008 Approved Employees	413.00
FY 2009 Mayor Changes	
<u>General Fund</u>	
Assessing - Appraiser	(1.00)
Community Planning - Planning & Zoning -Trails Coordinator	(1.00)
Community Planning - Platting & Mapping- Platting Officer II	(1.00)
Finance - Administrative Assistant	(1.00)
Land Management - Land Officer	(1.00)
Parks & Recreation - Parks Maintenance - Trails Planner	<u>1.00</u>
Subtotal:	(4.00)
FY 2009 Approved Employees	<u>409.00</u>

- Borough-wide, staffing decreased a net 4.50 full-time equivalent positions (FTEs) from FY 2008's Approved Budget of 376.11 FTEs.

<u>SUMMARY OF FTE CHANGES</u>	
FY 2008 Approved FTEs	376.11
FY 2009 Mayor Changes	
<u>General Fund</u>	
Assessing - Appraiser	(1.00)
Community Planning - Planning & Zoning -Trails Coordinator	(1.00)
Community Planning - Platting & Mapping- Platting Officer II	(1.00)
Emergency Service - Homeland Security Manager	(0.50)
Finance - Administrative Assistant	(1.00)
Land Management - Land Officer	(1.00)
Parks & Recreation - Parks Maintenance - Trails Planner	<u>1.00</u>
Subtotal:	(4.50)
FY 2009 Approved FTEs	<u>371.61</u>

Budget Highlights

Expenditure Highlights (Continued)

DEPARTMENT	2007/08 APPROVED BUDGET	CHANGES THRU 12/31/07	2007/08 REVISED BUDGET	ADJUSTMENTS TO PROGRAMS	2008/09 APPROVED BUDGET
Assembly	1,467,480	-	1,467,480	54,630	1,522,110
Mayor	1,293,940	-	1,293,940	25,250	1,319,190
Law	926,560	-	926,560	26,100	952,660
Assessing	2,507,960	-	2,507,960	(51,890)	2,456,070
Community Planning	1,967,030	-	1,967,030	(32,580)	1,934,450
Computer Services	2,841,930	-	2,841,930	467,550	3,309,480
Emergency Operations	4,474,680	-	4,474,680	442,230	4,916,910
Financial Services	4,369,346	(19,290)	4,350,056	34,484	4,384,540
General Services	1,475,760	-	1,475,760	(69,070)	1,406,690
Human Resources	2,760,710	-	2,760,710	(15,230)	2,745,480
Land Management	1,074,040	-	1,074,040	(80,750)	993,290
Library Services	4,871,470	-	4,871,470	157,990	5,029,460
Parks and Recreations	6,808,910	2,500	6,811,410	544,650	7,356,060
Public Works	17,086,810	-	17,086,810	573,580	17,660,390
Transportation	5,409,230	-	5,409,230	309,400	5,718,630
Education	42,222,700	-	42,222,700	2,000,000	44,222,700
Debt Service	16,587,710	-	16,587,710	(2,419,870)	14,167,840
Non-Departmental	547,640	-	547,640	(107,660)	439,980
Interfund Charges	2,967,420	-	2,967,420	190,320	3,157,740
Capital and Multi-Year Projects	4,754,760	-	4,754,760	(2,723,260)	2,031,500
Contributions to Fund Balance	408,650	-	408,650	675,230	1,083,880
	126,824,736	(16,790)	126,807,946	1,104	126,809,050

Summary of Major Changes in Expenditures from FY 2008

126,824,736

FY 2008 Approved Budget

2,500 Seasonal Donation

(19,290) Net adjustment Information Referral Grant

(16,790)

Total of Changes from FY 2008 Approved to FY 2008 Revised Budget

126,807,946

FY 2008 Revised Budget

(240,210) Other personnel changes and benefits

479,470 2.2% cost of living adjustment and union and management longevity adjustments

77,960 Overtime wages, temporary salaries and benefits

182,200 Benefit increases due to salary changes

2,000,000 Education increase

748,690 Fuel and Utilities increase

(2,419,870) School debt service decrease

301,180 Solid Waste Collection tipping and hauling fee increases

(723,260) Funding to Capital and Multi-Year Projects

(2,000,000) Funding to Facilities Major Maintenance Reserve Fund

(107,660) Non-Departmental

837,054 Other program cost adjustments, all funds and excludes salaries

190,320 Adjustment to Interfund Charges

675,230 Increase in Contributions to Fund Balance, net for all funds

1,104

Total of Changes from FY 2008 Revised to FY 2009 Budget

126,809,050

FY 2009 Approved Budget

Budget Highlights

Revenue Highlights

BOROUGH BUDGET REVENUE OVERVIEW

- The FY 2009 General Fund approved budget is \$6,940,851 under the Areawide Maximum Property Tax Computation.
- The FY 2009 operating budget is \$126,809,050. It is \$1,104 (see the detailed breakdown on page 27) more than the revised FY 2008's \$126,807,946 budget, and \$15,686 less than FY 2008's approved \$126,809,736.
- Property taxes: \$77,280,970 areawide, \$1,779,500 non-areawide, and \$5,242,200 solid waste collection district (\$84,302,670 combined) which make up 66.4% of the revenue budget, as compared to FY 2008 budget's \$83,801,560, and 66.1%.
- State revenues: \$10,835,530 vs. \$12,756,413 (FY 2008 approved budget); make up 8.54% of the revenues.
- Hotel-Motel Room taxes are projected to increase to \$1,690,000 from \$1,600,000 (FY 2008 approved estimate).
- In October 2003, the Borough voters approved the levy of a 5% Alcoholic Beverage Sales Tax. Alcoholic Beverage Sales taxes are projected to be \$1,380,000.
- In April 2004, the Borough Assembly approved the levy of an 8% Tobacco Distribution Excise Tax. Tobacco Distribution Excise taxes are projected to be \$1,000,000.
- Boroughwide budgeted interest earnings are projected to decrease from \$4,388,370 to \$2,716,330 from FY 2008's due to prevailing market conditions.

GENERAL FUND REVENUES

- The General Fund budget is \$104,794,140 which is \$1,323,040 less than FY 2008's revised \$106,071,653.
- Property tax revenues increased \$114,520 from FY 2008's \$77,166,450 to \$77,280,970 providing 73.7% of General Fund revenues.

Mill Rate Highlights

AREAWIDE MILL RATE/ASSESSED VALUES

- The (CY) 2008 mill rate is 11.287, or a (.922) decrease from the CY 2007 levy of 12.209. This reduction equates to a 7.55% decrease in the mill rate, making it the lowest rate since 1988.
- Levied areawide property taxes in the FY 2009 budget are \$77,597,940 (\$76,045,970 when adjusted for delinquencies); and \$100,080 less than FY 2008's \$77,698,020 (\$76,144,050 after delinquencies).
- Assessed valuation changes to "full taxable value": pipeline and associated personal property increased \$552,882,504; new construction added \$252 million and existing property valuations increased \$161 million. Combined with the exemption increases of \$42.3 million, the taxable assessed values increased from \$6.36 billion to \$6.87 billion.