BUDGET BRIEF

MILWAUKEE COUNTY

2024 EXECUTIVE BUDGET

WISCONSIN POLICY FORUM

ABOUT THE WISCONSIN POLICY FORUM

The Wisconsin Policy Forum was created on January 1, 2018, by the merger of the Milwaukee-based Public Policy Forum and the Madison-based Wisconsin Taxpayers Alliance. Throughout their lengthy histories, both organizations engaged in nonpartisan, independent research and civic education on fiscal and policy issues affecting state and local governments and school districts in Wisconsin. WPF is committed to those same activities and that spirit of nonpartisanship.

PREFACE AND ACKNOWLEDGMENTS

This report is intended to provide citizens and policymakers with an independent, comprehensive, and objective analysis of the Milwaukee County Executive's budget. We hope that policymakers and community leaders will use the report's findings to inform discussions during upcoming budget deliberations.

Report authors would like to thank officials and staff from the Milwaukee County Office of Strategy, Budget and Performance, the Comptroller's office, and the Milwaukee County Transit System for their assistance in providing information on the budget and the county's finances.

Finally, we wish to thank the Northwestern Mutual Foundation for generously supporting our local government finance research.

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Milwaukee County 2024 Executive Budget

October 2023

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INTRODUCTION

In the first sentence of his 2024 recommended budget, Milwaukee County Executive David Crowley notes that his number one priority since taking office was "to put Milwaukee County on the path to financial sustainability." He then proudly declares that "for the first time in decades, that goal has been achieved."

That is quite a bold statement from the leader of a government that has been struggling with annual budget deficits in the $20 million to $60 million range for the past two decades. But our review of the budget suggests it is not hyperbole.

The recommended budget not only avoids any noticeable cuts in services and staff, but it also makes tens of millions of dollars of important investments that will foster greater budget stability in future years. Even more astounding is its recommendation to reduce property taxes by a whopping $24 million – the first property tax reduction of any kind since 2004 and the first that has exceeded even a million dollars since at least 1992.

Even the capital budget – which has replaced the county's pension system as its most ominous financial challenge – benefits from an injection of nearly $31 million in cash financing and initiates major new projects in county parks and the Zoo. Looming on the horizon is the need to finance a new criminal courthouse, but planning for that project is initiated by setting aside $9.5 million in 2024.

This remarkable turnaround is linked primarily, of course, to the historic legislative package adopted in Madison this past summer. The new law – 2023 Wisconsin Act 12 – allowed county leaders to boost the county sales tax from 0.5% to 0.9% and provided an additional $7.6 million in state shared revenue for next year. But the county's good fortune also stems from the determination of county leaders to largely avoid the use of federal pandemic relief aids to temporarily fill operating budget gaps over the past two years as well as their continued build-up of reserves.

In the pages that follow, we detail the sea change in Milwaukee County's financial fortunes and what it means for county services and taxpayers. We also examine how long the county's newfound fiscal stability might last, and where its biggest financial troubles still lie. Our hope is to provide county policymakers and the public with impartial analysis and perspective on both the potential impacts of the 2024 budget and what it may foreshadow for the future.

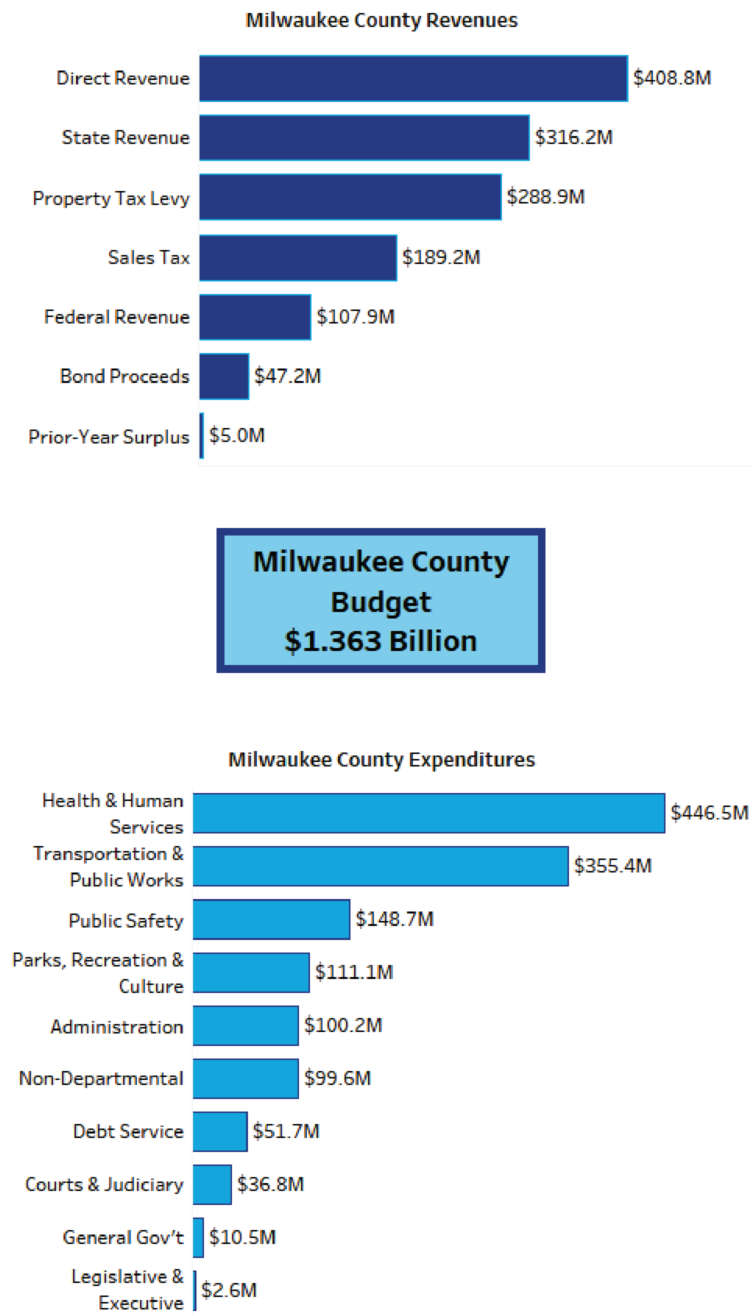
2024 RECOMMENDED BUDGET SYNOPSIS

The 2024 recommended budget totals $1.36 billion, a $10.7 million (0.8%) decrease from 2023. The decrease stems from a $73.0 million (37.0%) cut in the capital budget, from $197.0 million to $124.1 million. That cut is attributed to the much higher-than-normal nature of the 2023 capital budget, which included $113 million for a new forensic science center. The 2024 operating budget increases by $62.3 million (5.3%), from $1.18 billion to $1.24 billion.

Figure 1 breaks down the budget by major revenue and expenditure categories. As in previous years, the two largest spending areas are health and human services at $446.5 million (including $241.7 million for behavioral health) and transportation and public works at $355.4 million (including $145.2 million for transit operations). Public safety is next at $148.7 million.

The largest revenue source is "Direct Revenue" at $408.8 million, which includes service-related fees and payments such as zoo admissions fees, transit fares, and Medicaid reimbursement. State revenue is next at $316.2 million, overtaking the property tax levy, which is third at $288.9 million ($24.0 million less than 2023). The county also expects to receive $107.9 million from the federal government.

Figure 1: Summary of 2024 Recommended Budget (millions)



A major change in the county's revenues is the $189.2 million budgeted for the new 0.9% county sales tax. This is $90.4 million (91.6%) higher than the $98.8 million budgeted in 2023, when the sales tax stood at 0.5%. The additional 0.4% is projected to generate $84 million while collections from the pre-existing 0.5% sales tax increase by $6.4 million to just over $105 million.

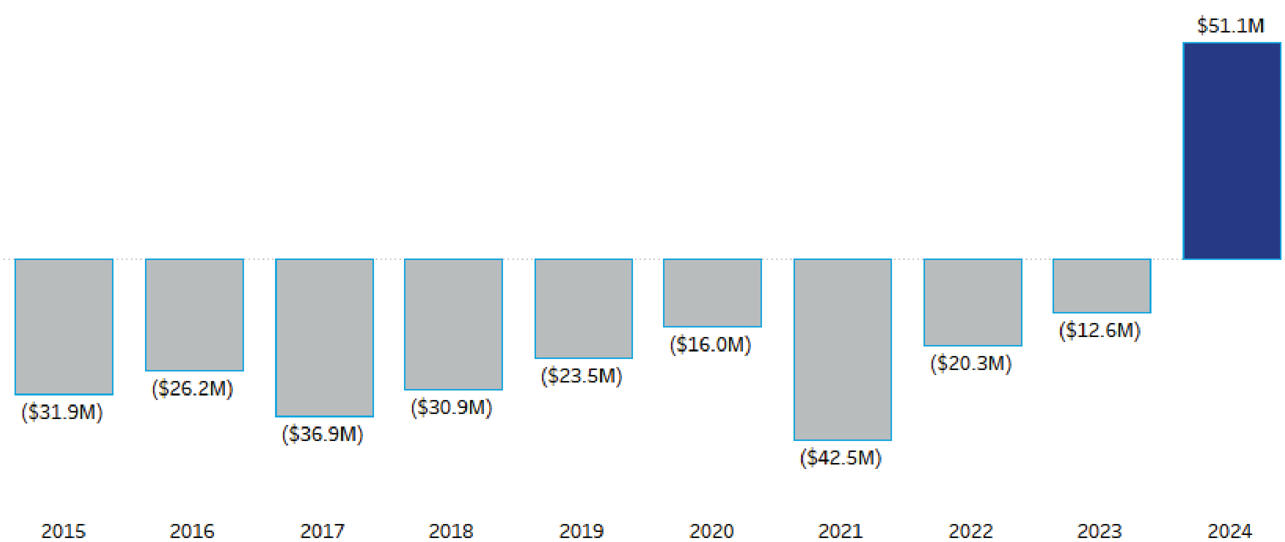
THE 2024 BUDGET SURPLUS

Every year since the Forum first began publishing Milwaukee County budget briefs in 2008, we have led off with analysis of the factors that created that year's budget gap and the key strategies used in the budget to bridge the gap. This year, we instead begin our report with a summary of how the county finds itself with a sizable budget *surplus* and discussion of how the county executive proposes to spend it in 2024.

The key to the surplus is the county's ability to begin collecting the additional 0.4% sales tax authorized by Act 12 on January 1, 2024 – a year before the exhaustion of monies from the federal American Rescue Plan Act (ARPA) would have created a huge hole in the Milwaukee County Transit System (MCTS) budget and converged with other long-time structural problems to create a sizable fiscal "cliff." As noted above, the expanded sales tax is budgeted to generate an additional $84 million in 2024, while Act 12's changes to the state shared revenue program will add $7.6 million.[1]

Act 12 also produces an added *cost* for the county by requiring the assumed rate of investment earnings on pension fund investments to decrease from the current 7.5% to 6.8%. This adds about $8 million to the required pension contribution for 2024.[2] Still, the net revenue increase of nearly $84 million produced by Act 12 not only eliminates the comptroller's originally projected $18.3 million gap for next year, but when combined with other pieces of good news leaves the county with an estimated "surplus" (per the county budget office) of $51.1 million to strategically invest plus $24 million for property tax relief. As shown in **Figure 2**, that presents a remarkable contrast to the previous nine years, when sizable budget deficits were a given.

Figure 2: Initial projected funding gaps or surpluses (nominal $ in millions)



Sources: Milwaukee County Comptroller's Office and Office of Performance, Strategy, and Budget. Note: The sizable increase in the funding gap shown in 2021 resulted largely from initial projections about pandemic-related revenue losses that did not fully materialize.

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[1] The county will see a total increase of $8.1 million in its state shared revenue allocation, as the component of the payment associated with utilities also rises by about $500,000.
[2] Other factors lower the total increase in the pension contribution to $4.9 million.

The other positive elements in the recommended budget – which likely would have wiped out most or all of the originally projected structural gap even without the passage of Act 12 – are the ability to budget an additional $13 million in **investment earnings** in light of higher interest rates and continued high levels of cash from ARPA and other sources; and the additional $6.4 million in revenue from the county's **current 0.5% sales tax**, which results from higher-than-budgeted projected collections in 2023 that provide a higher baseline from which to calculate an inflationary 3% increase.

Another remarkable factor is the continued **robust nature of the county's debt service reserve** (DSR). After a sizable ($21.7 million) year-end surplus in 2022 allowed for a $16.7 million contribution to the DSR earlier this year, its balance now stands at $108.2 million. Also, in part because of the investment earnings escalation cited above, the comptroller is projecting a surplus of nearly $36 million for 2023, which would allow the DSR to potentially grow by another $30 million or more next year. The recommended budget includes a DSR withdrawal of $11.8 million – $4.8 million to support the overall tax levy reduction and $7.0 million in one-time support for a capital project at the Zoo. The 2023 budget withdrew $7.8 million to free up debt service levy and $10 million as one-time support for the forensic science center capital project.

Finally, it should be noted that the county's ability to mostly refrain from using its $183.7 million ARPA allocation to fill holes in its 2022 and 2023 operating budgets pays off handsomely in the 2024 budget.[3] Without ARPA gaps to fill – outside of $2 million used in 2023 to boost corrections officer pay – the county executive and his budget team instead were free to use their unexpected sales tax and shared revenue bonus in 2024 for other priorities and strategic purposes.

How the surplus was used

The county executive and his budget team primarily employed the surplus to address three key priorities:

- **Property tax relief.** The recommended budget's property tax levy of $288.9 million is a $24.0 million (7.7%) reduction from the 2023 total of $312.9 million and marks the first time since 2004 that there has been a budgeted cut in the county levy (see Key #1 for further discussion). Prior to Act 12, it was anticipated that state-imposed levy limits would have allowed the county to levy up to a $4 million increase next year.

- **Meeting agency requests.** County departments generally received the funds they requested in their initial budgets last spring, as well as the dollars necessary to finance a 2% cost-of-living pay increase for most employees (at a total countywide cost of $4.5 million). It is important to note, however, that departments were instructed not to include any tax levy increase in their requested budgets, which means most had to find a way to absorb inflationary increases in items like commodities, supplies, contracts, etc. Certain departments and functions that have experienced particular financial challenges in recent years – such as parks – did receive increases aimed at shoring up staffing and service levels; and a few areas that have been prioritized by the county executive – including affordable housing – receive added funds. The budget also adds 64 full-time equivalent positions (FTEs) to the county workforce, including 22 in the administrative function (some of which replace contracted services).

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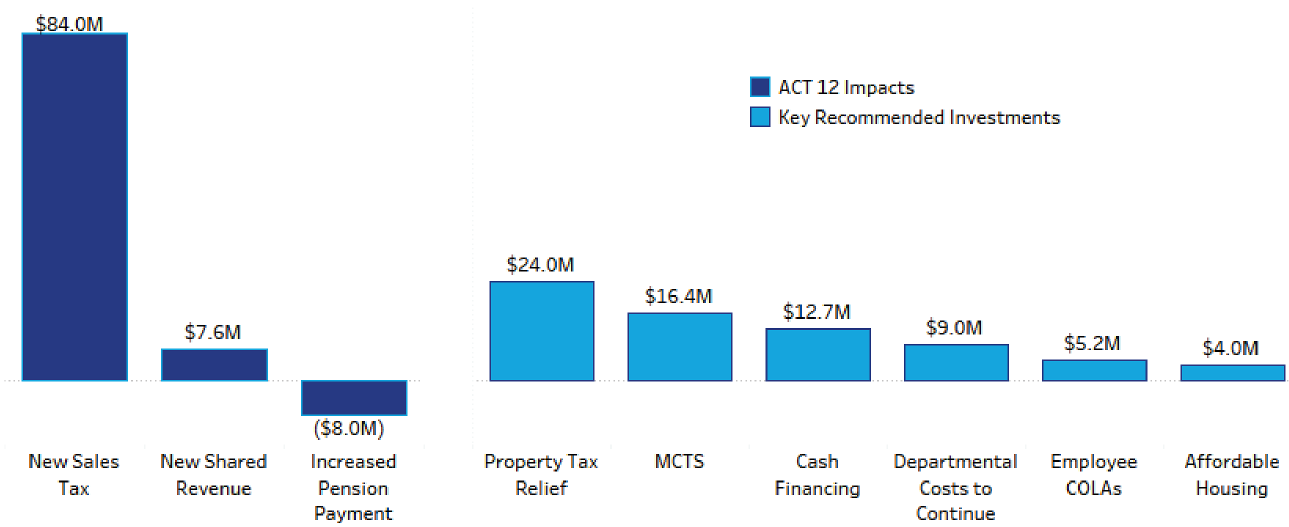
[3] The county *has* used separate special federal pandemic relief dollars totaling more than $190 million that were provided to MCTS to offset passenger revenue shortfalls per that intent, as we will discuss in Key #3.

- **Preparing for the future.** The budget recommends several strategic investments designed to make things easier for future budgets. The most notable of those – which we will discuss in detail later in the report – are increases of $16 million in property tax levy for MCTS, which allows the transit system to preserve $13 million in federal pandemic relief dollars for 2025 and 2026; and $12.7 million to escalate cash financing of capital projects, which serves the dual purpose of reducing the county's huge capital backlog and avoiding future interest payments on the debt that would have been issued for some of those projects.

There are dozens of recommended uses of surplus dollars sprinkled throughout the budget that aim to shore up areas of perceived budgetary weakness, enhance long-term fiscal sustainability, and even invest or reinvest in new priorities and positions. **Figure 3** shows that the areas of investment cited above account for $71 million in total additional investment that is made possible either directly or indirectly from the additional $83.6 million in net revenue generated by Act 12.

Figure 3: Act 12 impacts in 2024 vs. key recommended investments



Source: 2024 Recommended Budget (this or previous budget documents is the source for all other charts in the report unless otherwise noted)
Note: The $9.0 million cited in the figure for "Departmental Costs to Continue" comes from a rough estimate calculated by the comptroller's office earlier this year that budget officials say continues to represent a reasonable estimate.

Overall, the county's fiscal makeover not only provides policymakers with the ability to meet some priority needs in the upcoming budget, but it also allows them to take several steps to extend the fiscal good fortune into 2025 and future years. Balancing the desire to invest in priority service areas with the recognition that the county's structural imbalance may re-emerge without proper care is a central theme of this budget and one we will discuss in greater detail throughout this report.

OPERATING BUDGET OVERVIEW

The 2024 recommended operating budget totals $1.24 billion, an increase of $62.3 million (5.3%) over 2023. The budget changes the manner in which the county allocates centralized administrative costs (e.g. information technology, payroll, central accounting), which makes it difficult to compare proposed 2024 spending in functional areas with current spending.[4] Nevertheless, it is notable that the Health and Human Services and Public Safety functions both receive about $13 million above their 2023 totals and account for 42% of the countywide increase in expenditures.

The Public Safety increases are tied, in part, to a continuation of efforts initiated in previous budgets with ARPA dollars to enhance the pay of **corrections officers** in light of the county's difficulty with recruitment and retention for those positions. The cost of the contract with an outside vendor for medical care at corrections facilities also increases by $634,000, and $200,000 is added for a new initiative to provide housing vouchers for individuals being released from the Community Reintegration Center (CRC), formerly known as the House of Correction.

The Health and Human Services function sees a sizable ($6.7 million) increase for Behavioral Health Services, including an extra $1.1 million for substance use disorder services and an additional $1.3 million for crisis intervention services. Perhaps most notable, however, is the continued expansion of investment in the **Housing Division**, which receives $4 million for investments in affordable housing projects and $1 million for home repairs for seniors (both are cited as one-time investments) as well as an extra $700,000 for efforts to move unsheltered individuals off the streets. The Housing Division would receive $14.3 million in property tax levy in the recommended budget, which continues a gradual and substantial increase from the $2.0 million in the 2018 adopted budget.

The following are other specific areas of the operating budget that would see notable new or enhanced investment:

- The **Parks Department** would see expenditures increase by $2.5 million and tax levy by $694,000, primarily to support 18 additional FTEs. The new positions would allow the department to hire more full-time staff for maintenance activities given its challenges with hiring seasonal workers. While full-time positions have an added cost in terms of fringe benefits, the department cites a benefit in being able to both better retain such workers and to use them to catch up on deferred maintenance items in the winter months. The department also would receive $18.7 million for 11 parks-related projects in the capital budget.

- **Pretrial Services** would see a $1.7 million expenditure increase, from $5.4 million in 2023 to $7.1 million. Much of the increase is to meet inflationary growth in costs for contracted services for supervision and monitoring of individuals released pending trial, but it also would support enhanced case management for users of mental health and veterans treatment courts.

- The budget would replace $1.8 million in revenue derived from charges for **phone calls made by occupants at the Jail and CRC** with property tax levy, thus allowing most calls to be made free of charge. The intent is to allow occupants of the two facilities to better maintain connections to family members, which could help their eventual reintegration into society when released.

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[4] Budget officials say this change in accounting methodology will allow the county to draw down about $5.2 million in additional reimbursement from outside sources in the 2024 recommended budget.

- An appropriation of $3 million is provided to support salary increases that will result from an ongoing effort to **update pay grades and steps** for most positions in response to inflation and an historically tight labor market. While the funds for such moves are budgeted, requests to move specific positions to new pay grades will be submitted to the county board for approval. These dollars are recommended on top of the funds in agency budgets that will support the 2% cost-of-living adjustment (and 3% adjustment for corrections officers) noted earlier.

- The budget includes an additional tax levy appropriation of $2.0 million to pay off **uncollectable charges** to users of its County Grounds water system. The charges were an effort by the county to seek some reimbursement from other entities housed on the County Grounds for the cost of fire protection services provided by the city of Wauwatosa and billed to the county. Those users, however, have contested the charges and have not paid them, and for years the county budget has included a tax levy appropriation to offset the unpaid amounts. The extra $2 million would help the county to retire this outstanding liability in 2024 or 2025 under a new agreement with the city of Wauwatosa and would thus remove from future budgets the nearly $1 million annual tax levy appropriation that covered the uncollectable charges.

- About $1 million of surplus dollars are used to increase the contribution to the county's small **OBRA retirement system** for seasonal employees to bring the system up to a 100% funded level. In addition, the budget announces that the complete closure of the system will be considered in 2024 and an additional $870,000 is provided to potentially address costs associated with that move, which also would produce administrative savings.

Overall, the 2024 recommended operating budget avoids position cuts or service reductions and, even more encouraging, provides several million dollars for priority service enhancements and resolution of longstanding challenges in county operations. In our discussion below, we provide additional insight into the remaining areas of fiscal concern and the county's future budget outlook.

CAPITAL BUDGET OVERVIEW

For the second consecutive year, the recommended capital improvements budget would take a larger-than-normal bite out of the county's capital improvements backlog. Last year, however, that bite involved a decision to substantially exceed the county's self-imposed cap on borrowing to accommodate the new forensic science center, whereas in 2024 the budget would be bolstered with a sizable extra infusion of cash made possible by the budget surplus.

The capital improvements budget totals $124.1 million, which is a $72.9 million (37%) decrease from 2023. Of the total, $12.9 million is for projects at General Mitchell International Airport, which are fully reimbursed by airlines or outside revenue sources. Non-airport projects total $111.1 million, which is a decrease of $74.6 million (40%) compared to 2023. Again, both of these comparisons need to take into account the existence of the forensic science center project in the 2023 budget, which accounted for $112.9 million of the $197.0 million total capital budget.

The major source of capital financing is general obligation (G.O.) bond proceeds, which would total $47.1 million for non-airport projects in 2024. That total equals the amount allowed under the bonding limit, which was adopted by county leaders in the early 2000s to prevent an escalation of future debt payments and generally allows for a 3% increase each year.

More notable is the use of $30.8 million in property tax levy to cash finance some or all of 34 distinct projects. The use of cash reflects, in part, the fact that certain capital projects are ineligible for bond financing (often because their useful life does not exceed the life of the county's typical 15-year bonds). It is also a financial best practice for governments to complement borrowing with some degree of cash financing for capital improvements as a hedge against unhealthy levels of debt.

Milwaukee County has a cash financing goal of 20% of the cost of budgeted non-airport capital projects; to meet that goal in 2024, the budget would have needed $15.6 million of cash. By almost doubling that amount in the recommended budget, the county would be able to address a larger portion of requested projects in 2024 that are ineligible for bonding than it has typically been able to accommodate. In addition, cash that is used to support bond-eligible projects allows the county to avoid future interest payments that would have been required by borrowing. This is a particular advantage given today's high interest rates.

There are several notable major projects initiated in the 2024 recommended budget, including some that will have significant continued impacts on future capital budgets. Those include:

- **Bus Replacements** -- $21 million is appropriated for MCTS for 30 new buses. The county share is $4.2 million in bond proceeds, which equals the 20% local share required to match federal dollars. Similar appropriations will be required in future years if MCTS is to adhere to its goal of replacing roughly 25 to 30 buses annually.

- **Adventure Africa** – $12.5 million is included in the budget to initiate renovation of the rhino habitat at the Milwaukee County Zoo as part of the final phase of a multi-year Adventure Africa project. Notably, $7.0 million of that amount would be cash financed with funds withdrawn from the DSR – a one-time move that responds to a huge increase in the price of the project since it was first included in a 2013 master plan. At that time, it was anticipated that the Zoological Society would finance half the cost, but the price tag has grown from $10 million to $22.2 million due to inflation and new costs uncovered during the design process. The Society will devote $5.5

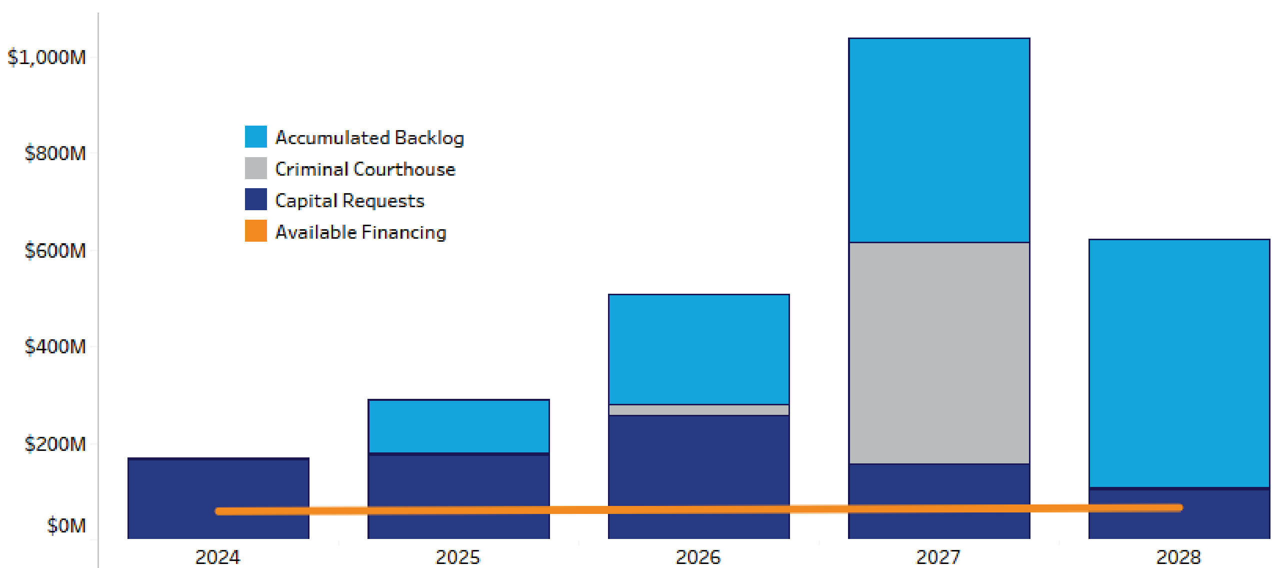
million to the project next year and the county will need to come up with another $9.2 million in 2025 to complete it.

- **South Shore Breakwater** – an appropriation of $11.3 million in G.O. bond proceeds would finance a major portion of a project to renovate and restore the breakwater that protects the shoreline and coastal assets along three lakefront parks. An additional $3.6 million will be required to complete the project in 2025.

- **New Criminal Courthouse** – the long-awaited replacement for the county's Safety Building (constructed in 1929) would be launched in 2024 with $9.5 million in cash financing for planning and design. We laid out financing options for a new criminal courthouse in a report published in 2018, when the estimated price tag was about $300 million. That cost has now grown to nearly $490 million due to inflation and further analysis, and additional appropriations of $20.5 million in 2026 and $458.5 million in 2027 are included in the five-year capital improvements plan. A plan to come up with those dollars has yet to be developed but as we noted in our 2018 report, it is difficult to imagine it taking place without help from the state.

The magnitude of these multi-year projects as well as dozens of others in the pipeline means that the infusion of cash financing in 2024 would provide only minimal relief for the county's long-term capital conundrum. As shown in **Figure 4**, the amount of borrowing and cash that would be available under the bonding limit and 20% cash financing goal in each year of the county's five-year capital plan pales in comparison to the cost of projects already requested by departments. Consequently, a capital backlog estimated at close to $1 billion almost certainly will continue to grow.

Figure 4: Available county financing vs. non-airport capital requests, 2024-2028



Source: 2024 Recommended Capital Improvements Budget

In the wake of Act 12, the county's huge backlog of pending capital projects now undoubtedly constitutes its foremost fiscal challenge. Fortunately, the county may now have the financial capacity to re-examine and possibly increase the bonding cap. It still would appear to be an immense challenge, however, for it to be able to devise a long-term capital financing plan that would be both affordable from a debt service perspective and capable of meeting all of its capital needs (see Key #4 for further discussion).

FOUR KEYS TO THE 2024 RECOMMENDED BUDGET

Key #1: A property tax *cut*

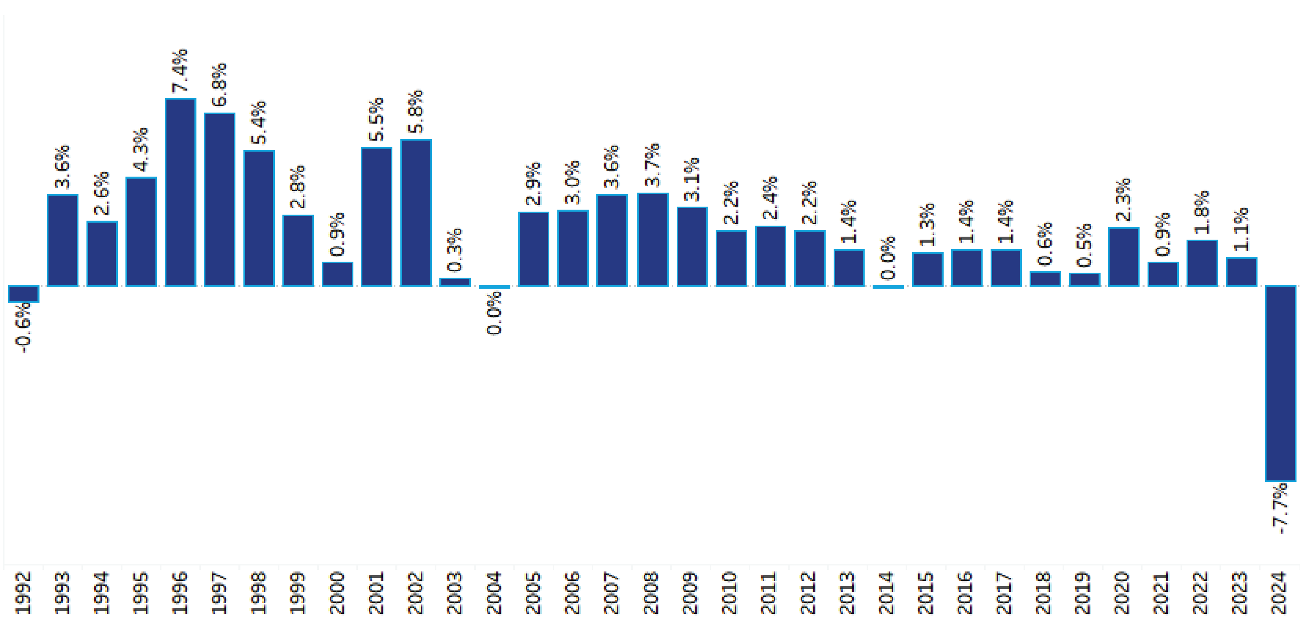
In our 2017 report on the city of Milwaukee's "broken" revenue structure (*On the Money?*), we argued that the case for adding a sales tax to the city's revenue mix should be predicated not only on its need for more revenue, but also on a desire to promote greater diversity and equity in the city's local tax structure. As we pointed out at the time:

> *Milwaukee's property owners and residents bear the bulk of the financial burden for Wisconsin's flagship city. Their property-related taxes and fees are the sole source of locally-generated support for municipal infrastructure and services that are critical to employment and entertainment for nonresidents, who pay no local taxes to the city.*

Implicit in our argument – which also could be applied to Milwaukee County government given its only somewhat more modest reliance on property taxes and the number of non-county residents who benefit from its services daily – was that a reformed local tax structure ideally would use some of the new sales tax revenues to offer at least some property tax relief to residents. In fact, each of the four hypothetical revised local tax structures we modeled for in our 2017 report included sizable reductions in property taxes to offset some of the burden for city residents of new sales taxes.

While the 2024 proposed budget for the city of Milwaukee was unable to deliver such property tax relief in conjunction with its new sales tax, the county's ability to do so is a striking development. The $24 million (7.7%) property tax levy reduction would be the first reduction of any kind since 2004 and the first of any magnitude since at least 1992 and likely much further back (see **Figure 5**). The cut lowers the county's property tax *rate* from $3.60 per $1,000 of assessed value to $3.01, producing a $101 tax savings for the owner of a median-valued county home of $172,000.

Figure 5: Percent change in budgeted property tax levy, 1992-2024



The provision of such extensive property tax relief was based on both desire and necessity. According to an October 4 memo issued by the comptroller, the state requirement that sales tax revenues must be used to pay both the employer contribution for unfunded pension liabilities *and* the required debt service payment on the county's pension obligation bonds (POBs) has a significant impact on the county's state-imposed levy limit in 2024.

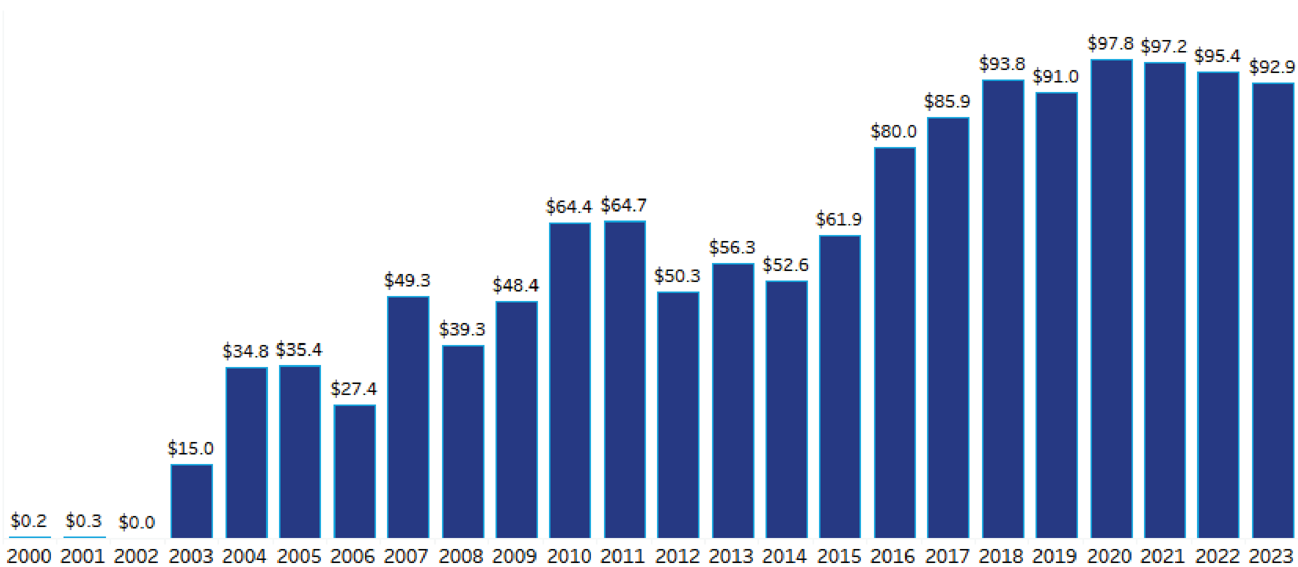
The memo indicates that the proposed use of $23.4 million in sales tax to pay POB debt service – when combined with other typical levy limit adjustments – requires the county to lower its property tax levy by $19.2 million. The budget exceeds that amount by nearly $5 million with its proposed $24.0 million reduction.

Regardless of whether the recommended property tax relief stems from prioritization or legal necessity, **it is a significant benefit for county property owners and helps offset some of the financial sting associated with both the new city and county sales taxes.** As we discuss later in this report, property tax relief may turn out to be a one-time occurrence given that the county's structural challenges are likely to soon re-emerge. Still, the benefit to taxpayers from the recommended cut would extend for some time assuming that the state levy limits remain in place, as future allowable increases in the county's levy will be applied to a base of $288.9 million (the recommended levy for 2024) rather than the 2023 base of $312.9 million.

Key #2: Pension pressures are easing

There once was a time when Milwaukee County had an "overfunded" Employee Retirement System (ERS), which means its pension fund assets exceeded the value of its actuarially-determined long-term liabilities. Consequently, no or very little property tax levy support was needed outside of amounts for system administration. Unfortunately, the last time that occurred was in the 2002 budget, which was adopted in the fall of 2001 – a few months before the impacts of a lucrative pension enhancement package adopted earlier that year were discovered.

Figure 6: Annual required employer pension contributions (in millions)



Source: Milwaukee County Comptroller's Office

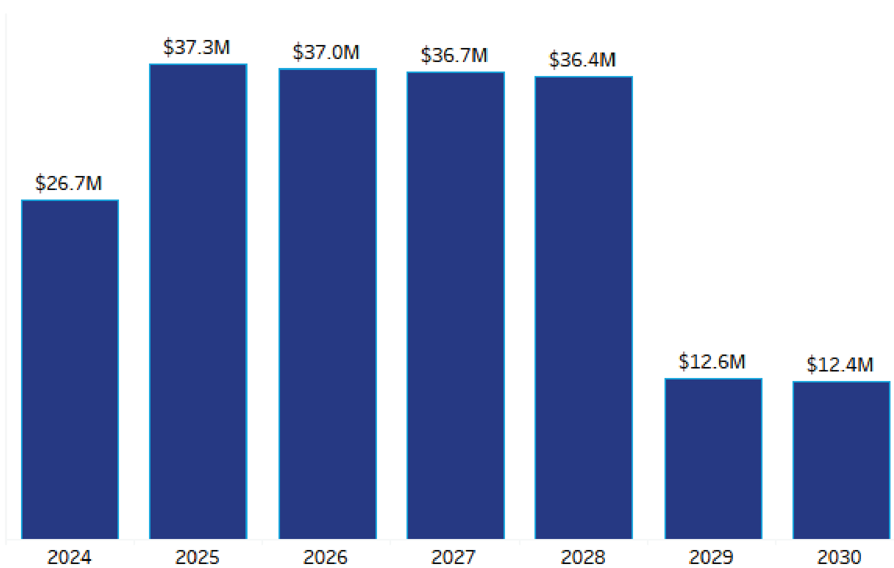
From that time, as shown in **Figure 6** on the previous page, required employer pension payments increased rapidly, with annual totals mostly ranging from $35 million to $50 million for the rest of the decade. They jumped again in 2010 to about $64 million, before stabilizing for a few years as the positive impacts of a decision to issue $400 million of pension obligation bonds (POBs) came into effect. The bonds substantially reduced the county's unfunded pension liability and the volatility of payments associated with that liability – which fluctuate annually based on the previous year's investment returns – by allowing it instead to make consistent annual debt service payments of about $33 million. Also, the adoption of 2011 Wisconsin Act 10, which required *employees* to make pension contributions, further helped to control the employer contribution beginning in 2012.

As shown in the figure, contributions then continued their ascent in the middle of the decade (though at a slower trajectory) and peaked in 2020. The main culprits were lagging investment returns and other factors (like lengthier lifespans) that led actuaries to project greater potential liabilities in the future and to recommend larger taxpayer contributions to address them.

The history of the $90 million-plus property tax levy-funded pension contributions ends, however, with the implementation of Wisconsin Act 12. In the recommended budget, $60.6 million of the $84 million in projected new sales tax collections would offset the actuarially determined employer contribution for the unfunded liability, while the remaining $23.4 million pays all but $3.2 million of required POB debt service.[5] That $3.2 million – combined with $22.9 million to fund the retirement system's "normal cost" for 2024 – produces a tax levy contribution of "only" $26.1 million for the ERS next year.

This development should not be confused with a reduction in overall pension costs, which are still steep. Rather, the critical change is that the county finally has a dedicated funding source to address its pension obligations in the form of the sales tax, which gives it the ability to use the bulk of its property tax levy resources for core services, instead of using a quarter to a third for pensions.

Figure 7: Scheduled remaining POB debt service payments



Source: Milwaukee County Comptroller's Office

[5] The debt service payment declines by about $7 million in 2024 due to a quirk in the debt service schedule but will escalate back to $37 million (about $4 million higher than previous amounts) in 2025. Also, the 2024 reduction in the POB debt service payment is completely offset by the previously mentioned $8 million increase in the unfunded liability payment that is caused by an Act 12 requirement that the county lower its assumed rate of pension fund investment earnings. Finally, it is important to note that Act 12 requires the new sales tax to sunset after the ERS is fully funded (i.e. its actuarial liabilities are eliminated) or 30 years after it takes effect, whichever comes first.

There is even better news on the horizon. While the contribution for the unfunded liability still will be subject to volatility and could increase depending on investment returns and other factors, the POB debt service payment will decline considerably in 2029 and will be wiped off the county's books entirely after 2030 (as shown in **Figure 7** on the previous page). That will create new opportunity for substantial reinvestment in other priorities five years from now. Also, Act 12's stipulation that new employees enroll in the Wisconsin Retirement System instead of ERS will produce even greater long-term stability.

The need to contribute more than $90 million annually from local revenue sources for pension liabilities still poses a major challenge for the county. However, it reaches a once unimaginable achievement in 2024 as its property tax obligation for the employer contribution falls to a level not seen since 2003, with promise of future reductions beginning five years from now. That milestone – which frees up more than $65 million of property tax levy for core services like public safety, parks, and transit -- is one that should not go unnoticed by county residents.

Key #3: Transit cliff is pushed down the road

Earlier this year, in *Detour Ahead*, we sized up MCTS's oncoming "fiscal cliff" and options to avert it. We posited that by 2025, when MCTS's $191 million of special federal pandemic relief aids were projected to be exhausted, it would face "a sizable gap" of between $17.9 million and $25.7 million. That gap would necessitate substantial service reductions if fixes did not emerge.

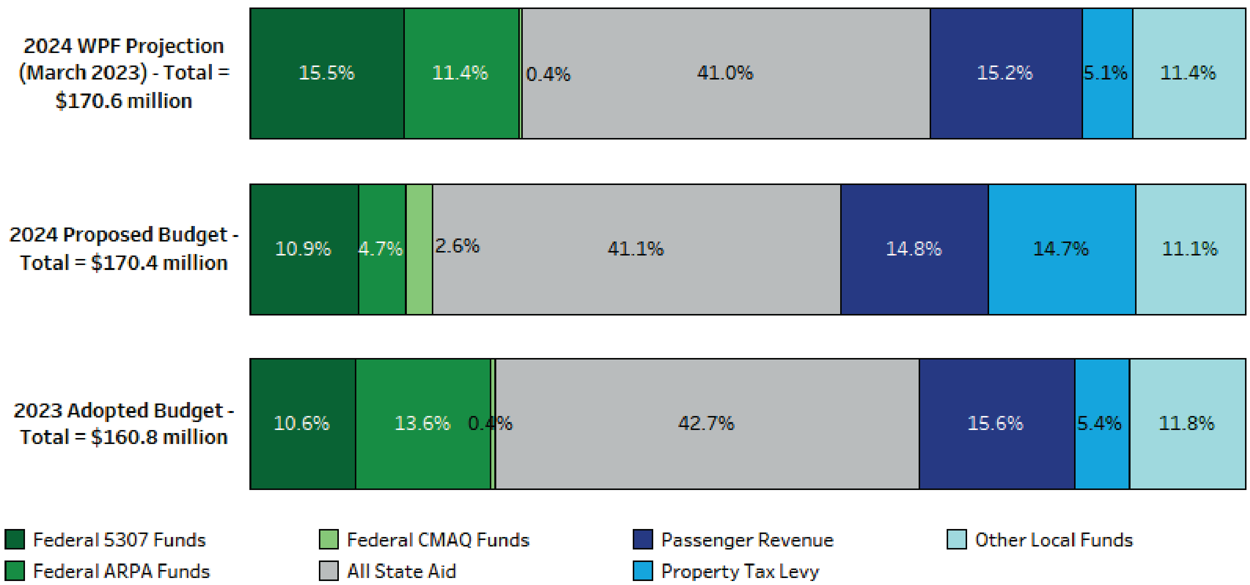
One of the possible fixes we cited was a state-authorized increase in the county's 0.5% sales tax, which has since been delivered with the passage of Act 12. We pointed out that even with such a move, however, it was uncertain how big a portion of any new sales tax collections (or property tax dollars freed up by them) would be allocated to transit given the county's other pressing needs. For modeling purposes, we hypothetically assumed one tenth of the $95 million the county would receive from doubling the sales tax ($9.5 million) would be directed annually to MCTS, which would have eliminated the fiscal gap through 2028 when combined with other assumptions.

Notably, those other assumptions included doubling from $30 to $60 the county's vehicle registration fee (VRF) over three years and a 2% increase in state transit aids in the first year of each of the next three state budgets. And even with that combination, we noted that "MCTS's improved fiscal outlook would deteriorate over time…(and) deficits ultimately would emerge once again in light of a continued structural imbalance."

The recommended budget answers the question of how much a new sales tax might benefit MCTS in an encouraging way for transit users and advocates. Compared to just $8.7 million in property tax revenues in the department's 2023 budget, the county executive is proposing the use of $25.1 million in 2024. That would be the largest amount of property taxes used to fund transit since 2016 – the year before the county adopted its $30 VRF and used those revenues to back out a significant portion of its property tax levy. It would mean the property tax would fund 14.7% of MCTS's budget in 2024, as compared to just 5.4% this year (see **Figure 8** on the next page), and it would also allow for a $1.3 million investment in enhanced transit security services.

The infusion of property tax levy is made possible by the more than $65 million of levy that is no longer necessary for the county's pension contribution and is freed up for other uses. MCTS would receive about a quarter of that amount, which compares favorably to the one-tenth of new sales tax revenues we modeled in our March report. MCTS also did receive a 2% increase in its state operating assistance for 2024 per our model, while the VRF remains at $30.

Figure 8: Source of Funds for Milwaukee County Transit System



The infusion of levy and, to a lesser extent, the extra state aid allow the county to be strategic in its use of other operating revenues. Specifically, substantial portions of two critical types of federal aid would be "banked" for use in future years.

MCTS receives a sizable allotment each year on a formula basis from the federal government. While available for capital spending only, these so-called "5307 funds" also can be used for up to 80% of the cost of maintenance activities in the operating budget. We estimated in March that MCTS would receive about $25 million in 5307 funds in 2023, with increases of about 2% to 3% each year through at least 2026. The recommended budget would use $18.6 million of these funds for operations in 2024, leaving roughly $6.4 million available for capital needs or future budgets. MCTS also holds a sizable reserve of 5307 dollars that it has accumulated in recent years, and those monies would be used for the 80% federal share of new bus purchases contained in the recommended capital budget.

The decision to boost MCTS's property tax levy by $16.4 million also allows it to reduce to $8 million the amount of ARPA monies used in the operating budget and preserve roughly $12.5 million remaining from ARPA to spread equally in the 2025 and 2026 budgets.[6] In the 2023 budget, policymakers used $21.8 million from this same source (13.6% of MCTS's revenue), and MCTS officials originally anticipated that most or all of the approximately $21 million remaining would need to be used to preserve existing service levels in 2024.

Another piece of good news for MCTS's budget is an increase in revenues from the federal Congestion Mitigation and Air Quality (CMAQ) Improvement Program. The budget includes $4.5 million of CMAQ funds to support operating and marketing costs associated with new Bus Rapid Transit (BRT) service in the first installment of a $6 million two-year grant.

On the negative side, the recommended budget projects $25.2 million in fixed route ridership revenue, an increase of just 0.6% over the 2023 budget. While passenger revenues have recovered

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[6] The ARPA dollars for transit must be obligated by the end of 2024 but can be spent through 2026.

somewhat from a low of just $16.8 million in 2020, they are well below the $30.8 million that was generated prior to the pandemic in 2019, and even further below revenues from earlier that decade.

Still, despite the continuing challenge of reduced ridership, **MCTS's outlook appears stable at least through 2026 *if* the county is able to maintain the current property tax levy commitment**, as the banked federal funds plus the potential to use more of the 5307 monies in future years for operations should give it capacity to meet costs to continue. Still, the warning we issued in March still holds – by later in this decade, MCTS's structural hole almost certainly will re-emerge, which may necessitate VRF increases, service cuts, or both unless passenger revenue recovers or other solutions are identified.

Key #4: Will the good times last?

Since the adoption of Act 12 this past summer, Milwaukee County officials have cautioned fellow policymakers and citizens to tone down their excitement. Specifically, they have warned that while the infusion of new revenues would eliminate the anticipated deficit for 2024 and the more concerning fiscal cliff in 2025, the county's structural imbalance had not been fully reconciled and a sizable budget deficit would re-emerge by 2026.

Our take, now that we have reviewed the first post-Act 12 recommended budget, is that the county will be in even better shape to manage the return of its operating budget challenges two years from now than we had previously thought. That encouraging prognosis is tempered, however, by the outlook for the capital budget, which is every bit as dire as it was at this time last year.

The comptroller's latest five-year fiscal forecast – updated after the passage of Act 12 – projects that after experiencing a sizable surplus in 2024 and a smaller one ($2.7 million) in 2025, the county will experience an operating deficit of $13.0 million in 2026 that will grow to $36.2 million by 2028. The return of these gaps is based on a projection that despite the county's more robust revenue sources, annual cost-to-continue expenditure needs will still outpace annual revenue growth, producing a lingering structural hole that will grow by an average of $12 million per year over the five-year period.

Those projections, however, need to be considered with some important context. The forecast is very useful in determining *if* there is a structural imbalance between projected expenditure needs and revenue growth, as well as the approximate annual size of that imbalance over the forecast period if no permanent actions are taken to address it. However, when deficits actually occur, the county *must* take steps to resolve them and produce a balanced budget. Often, those steps can be one-time in nature, but it is also quite likely that at least some will involve permanent expenditure reductions or revenue increases that will positively impact the structural imbalance in the years ahead.

In light of the sizable surplus, the recommended budget did not need to include permanent expenditure reductions or revenue increases. In fact, the budget adds dozens of positions that may exacerbate structural challenges to some extent. However, as previously discussed, the budget also takes several important steps that will temper future operating budget challenges and provide additional tools to manage future gaps. Those include:

- **More tax levy for MCTS.** The previously discussed addition of $16.4 million of property tax levy in MCTS's budget not only eliminates the need for service reductions next year, but also creates greater flexibility by preserving both ARPA and 5307 funding for use in future budgets. At minimum, that cushion should preclude the need for *additional* tax levy in the transit budget through at least 2026, thus relieving a key expenditure pressure in the budget through that date.

It also may allow officials to again reduce the tax levy allocation in future years and offset such reductions with federal dollars.

- **Cash financing capital improvements.** As discussed earlier, the sizable surplus in 2024 allows the budget to exceed the typical 20% cash financing goal for the capital budget by $15.2 million. While budget officials undoubtedly would like to appropriate similar cash amounts in the future to finance capital projects that are not eligible for bonding, they do have leeway to redirect some or all of that $15.2 million to operations in future budgets.

- **Eliminating or reducing long-term obligations.** The steps referenced earlier to close out the OBRA retirement system and settle outstanding fire service obligations to Wauwatosa ultimately could save the county combined expenditures of about $1.1 million annually in future budgets.

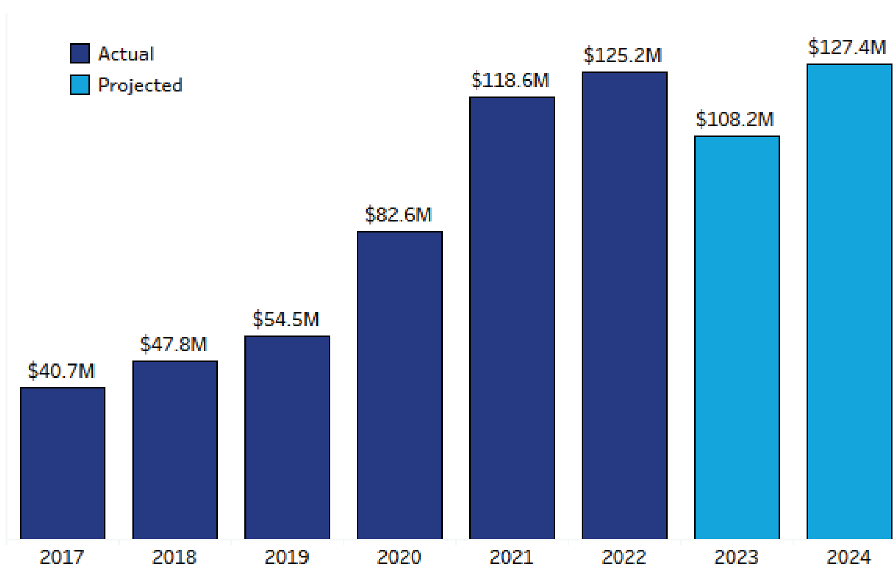
- **One-time levy funds for housing.** The recommended budget includes $4 million for several investments in affordable housing and $1 million for home repairs for seniors that are labeled as one-time investments. That total of $5 million would be available to shift to other priorities or general operations after 2024.

Perhaps most important for the future, the county is well-placed to make **sizable draws from the Debt Service Reserve** in future years. As noted earlier, a $36 million projected year-end surplus for 2023 should allow the DSR to grow substantially next year – perhaps adding nearly $20 million to the current hefty balance of $108.2 million even after a draw of $11.8 million in 2024 (see **Figure 9**). Also, $7 million of the withdrawal would cash finance the rhino capital project at the Zoo, and those funds could potentially be shifted to support the operating budget in the future (this would be part of the reduction in cash financing noted above).

On the negative side, the need to service the sizable amount of debt that has or will be issued for the forensic science center and the county's contribution toward a new Milwaukee Public Museum building will produce a sizable increase in future debt pay payments. Those may necessitate larger draws from the DSR to ease the impact on the property tax levy, and not for operations.

The county has not updated its policy goal for an appropriate DSR balance for several years. Still, given the impressive growth in the balance over the past several years, it appears likely that it will be able to responsibly maintain withdrawals in the $10 million to $12 million range for at least a few years to support general operations, and that the withdrawal even could be reasonably increased if necessary in the short term to address the

Figure 9: Debt service reserve year-end fund balance, 2017-2024



Sources: Milwaukee County Comptroller's Office and WPF projections increase in debt service from major projects or any unforeseen needs that arise as the Act 12 benefits begin to wane over time.

Overall, it is far too early to reliably prognosticate the county's operating budget prospects past 2024 or 2025. Still, when combined with the likelihood of future growth in state shared revenues due to their linkage to state sales tax collections – as well as greater growth in the county's own sales tax collections given the larger size of the tax and a return to annual 2% to 3% property tax levy increases – **the factors discussed above would appear to give county officials sufficient tools to manage potential deficits without having to resort to widespread budget cuts for at least the next two to three years**. And, if that manageability could possibly be stretched to 2029, then they would receive another big boost from declining POB debt service to potentially extend the good times even further.

Lurking beneath this encouraging outlook, however, are a couple of important questions. The first involves the continued high numbers of vacancies sprinkled throughout county departments, which have helped generate recent impressive year-end surpluses and may only be temporarily holding down spending on employee health care.[7] A key question is whether many of those positions ultimately will need to be filled – in which case the county may need to again budget for sizable annual health care increases and reduce vacancy savings included in the recommended budget – or whether departments have found ways to operate effectively without them.

An even more pressing question involves the capital budget. As discussed earlier, a backlog of needed capital projects has been building for years as the county has sought to limit annual borrowing to drive down debt service costs. While the effort to reduce debt payments has been quite successful, the capital project backlog is now estimated at nearly $1 billion when the new criminal courthouse facility is included.

Despite the accumulation of this backlog over many years, the county still lacks a plan to address it. It would seem that a first step is to re-examine what is an affordable level of county borrowing in light of the revenue enhancements produced by Act 12 and the arguably over-funded DSR. However, while that step may well determine that the self-imposed bond limits could be adjusted upwards, the impact of higher interest rates and inflation-affected construction costs means that fewer projects can be squeezed within those limits, even if they are raised. Moreover, a substantial increase in borrowing may not be enough to significantly erode the backlog given the number of new projects that arise each year.

It also should be recognized that increased borrowing is a double-edged sword. While it could allow the county to take care of more capital needs, the rise in levy-supported debt service payments that would accrue over time could dampen the willingness of policymakers to increase property taxes for operations even when allowed to do so under state levy limits.

The bottom line is that Milwaukee County leaders now seem to have achieved more stable operating budgets than they have had in a generation. Whether that stability now positions them to be able to formulate a workable plan for addressing their seemingly insurmountable capital challenges is the most important financial question remaining for the next few years, and it is a doozy.

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[7] Gross employee/retiree health and dental costs are actually reduced by $492,000 from the 2023 budgeted amount in the recommended budget.

CONCLUSION

The 2024 recommended budget marks the dawning of a new day for Milwaukee County – one in which the need to choose among a menu of undesirable budget cuts each year is replaced, at least in the near term, with an opportunity to consider new investments to better meet the needs of residents and improve the county's long-term financial picture.

This opportunity is far more pronounced in the 2024 budget than it will be in future budgets given the chance to collect revenues from the expanded sales tax a year before the arrival of a dreaded fiscal cliff. The county executive takes advantage of it by boosting services for parks and housing, investing more property tax resources in transit and capital projects to alleviate future challenges in those areas, and doling out a larger-than-required property tax reduction to offset some of the impact of the increased sales tax.

Yet, while several immediate challenges and priorities are addressed and the county's deficit reduction toolbox has been fortified, the immense capital backlog shows that its financial problems are far from fully behind it. Meanwhile, the impacts of high inflation and the possibility that dozens of vacant positions will need to be filled and funded create additional concerns.

Indeed, county policymakers would be wise to see their good fortune as a well-deserved but short-term reprieve, and to use the next couple of relatively calm years to develop a plan for the capital backlog. This time also should be used to intensify efforts to pursue money-saving service sharing and consolidation opportunities with Milwaukee's city government and other local jurisdictions, and to continue and even expand the efforts undertaken over the past decade to right-size the county's physical footprint and identify operational efficiencies.

It would be difficult to blame county leaders for basking in their dramatic and unprecedented budgetary improvement and delaying, for now, their worries about tomorrow. Yet, as budget deliberations continue, they should also remember the words of famed musician Bob Marley, who once sang that "in this bright future you can't forget your past."