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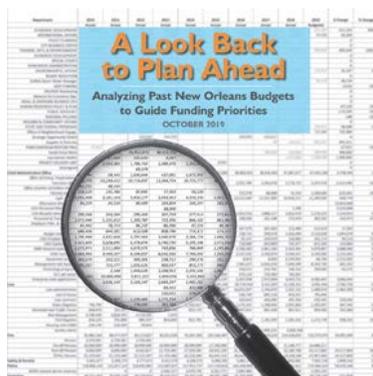
Applying BGR Research to Public Policy Issues
in the New Orleans Area

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Welcome to the inaugural edition of *PolicyWatch*, a periodic newsletter that draws on BGR’s body of independent, nonpartisan research to address current public policy issues. This edition focuses on the City of New Orleans’ finances as it faces a pandemic-induced budget deficit. It discusses the City’s proposal to borrow up to \$100 million as well as other options to address the deficit by cutting costs. It is critical that the City’s fiscal decisions in the coming weeks and months work toward the long-term sustainability of City operations and functions, especially those addressing high-priority needs.

Amy L. Glovinsky, President & CEO
Samuel Zemurray Chair in Research Leadership

In This Edition...



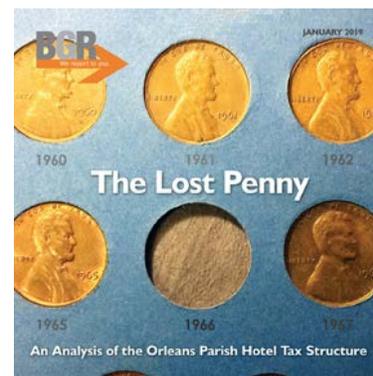
OFFSETTING THE CITY BUDGET DEFICIT

BGR urges the City of New Orleans to plan its post-pandemic fiscal recovery carefully and



CITY COUNCIL REVIEWS REVENUE

Prior to the public health crisis, a New Orleans City Council committee followed through on



LOST PENNY RESTORED

Infrastructure in New Orleans will see a long-term funding increase from last year’s action by

exhaust other options before borrowing up to \$100 million to help offset its deficit.

BGR's call to study tax dedications and issued revenue-generating recommendations.

the State Legislature to restore a long-suspended 1% hotel tax as BGR recommended.

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Borrowing Proposal Carries Risks; City Must Exhaust Other Options to Offset Deficit

As New Orleans leaders respond to the ongoing public health crisis, they are also grappling with the growing fiscal challenge it poses. City administrators announced in early May that the City faces a projected deficit of \$130 million to \$170 million, or 18% to 23% of its \$726 million General Fund operating budget. This is largely due to a sharp reduction in sales and hotel tax receipts from business closures to contain the spread of the coronavirus.



The City's projections appear to be in line with those in a May 7 Louisiana Legislative Auditor's report. It estimates New Orleans will see, in an average recovery scenario, a \$109 million reduction in sales, property and hotel taxes through June 2021. While this estimate is lower than the City's and covers a longer time period, it excludes some revenue streams – such as service charges, fines and grants – that account for about 40% of the City's General Fund revenues. The City's estimate also factors in \$20 million in unbudgeted pandemic-related expenses that are not included in the legislative auditor's projection.

City administrators estimate that a partial hiring freeze will save about \$16.7 million, while other potential cost-cutting measures could save an additional \$10 million to \$15 million. But this would still leave a large projected deficit. The administrators are working to secure federal aid to help bridge the shortfall. In the meantime, they have proposed borrowing up to \$100 million through a line of credit that the City could draw upon as needed to close budget gaps. The interest rate would be capped at 6%, and the repayment period could not exceed 15 years.

The City Council gave preliminary approval to the proposed borrowing on May 7. Today, the Louisiana State Bond Commission authorized the City to proceed with the borrowing. The City has set a May 28 deadline to receive loan proposals from financial institutions, with funds to be available by July 1. The City Council would have to approve the final loan terms.

City administrators said that drawing from the line of credit would be a last resort after they exhausted other measures to deal with the fiscal crisis. In a filing with the bond commission, the City said these measures include the hiring freeze, early retirement incentives, implementation of a city-wide budget reduction plan, evaluation of service reductions and reduction of budgeted overtime. The City's chief financial officer said that while the economic downturn is expected to persist beyond 2020, the City does not plan to seek approval for additional loans.

The City has not finalized key details of the proposal, including the specific circumstances under which it would tap the line of credit and for what purposes. Providing clear answers to those questions is essential for good stewardship of taxpayer funds. Borrowing money to cover recurring operating expenses carries risks as the City would have to pay the money back plus interest in subsequent years. Administrators estimated repaying the loan would cost about \$9 million a year for 15 years. That is money that the City could otherwise use to address high-priority needs or deal with the pandemic's continuing financial repercussions.

In authorizing the City to move forward with the proposal, several members of the bond commission expressed concerns about it. They said a 15-year repayment period for a loan to cover operating expenses is unprecedented and could be a drag on the City's finances. They urged the City to avoid using the loan to defer tough decisions on necessary budget cuts.

After Hurricane Katrina, the City borrowed a total of \$240 million from the federal government over five years to help offset deficits. However, the loans were ultimately forgiven, and the City did not have to pay back the money. The City would have to repay the proposed loan with future City revenues unless it received State or federal aid to do so.

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There is much the City would have to do to demonstrate that it had exhausted all appropriate cost-cutting measures before tapping the proposed line of credit. In the wake of the Great Recession that started in 2008, government finance experts have done extensive research on recovering from fiscal crises, establishing comprehensive recommendations for local governments on the recovery process. For instance, the Government Finance Officers Association (GFOA) developed a [12-step process](#) that it has updated in response to the specific circumstances of the coronavirus pandemic. It includes a mix of short-term, smartly executed cutbacks followed by longer-term planning, adaptation and reserve building. Driving the entire process is a systemwide commitment to frugality, efficiency, data-driven analysis and citizen engagement.

The GFOA does not specifically discuss the type of borrowing the City is considering: a 15-year bank loan backed by the City's general purpose property tax receipts. However, it advises governments to use "extreme caution" in employing another emergency borrowing approach: a short-term loan backed by

anticipated tax receipts. It cites a general best practice to avoid paying interest on funds for operating expenses. It also cautions that future tax revenues might be less than expected as a result of the pandemic, making it more difficult to pay off the debt. This raises the bar on what the City must do to show that the borrowing proposal is an appropriate strategy.

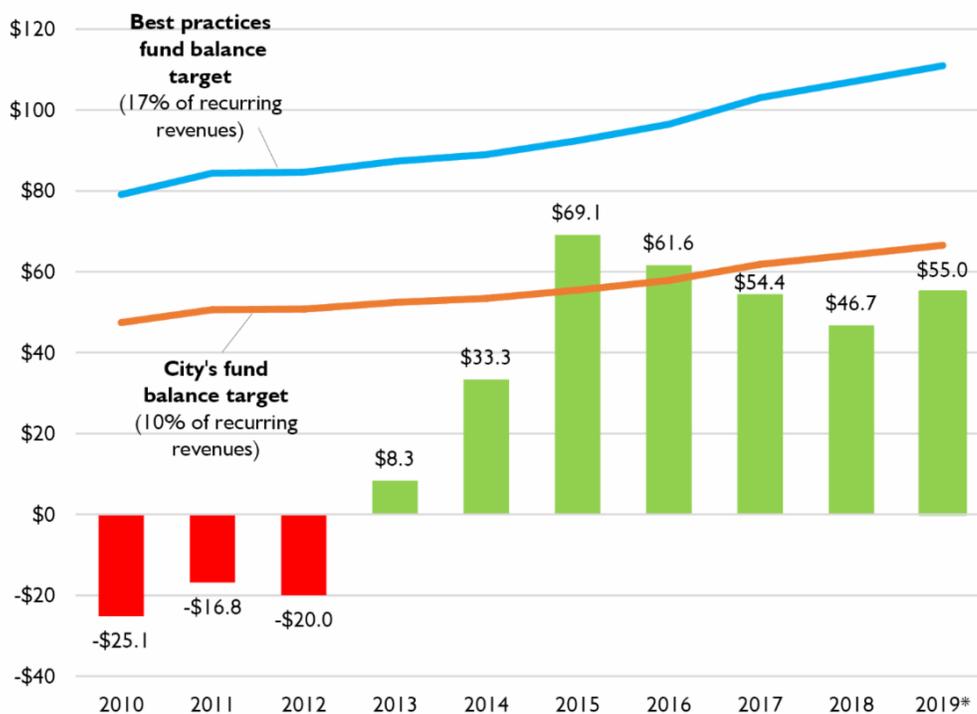
The GFOA recommends that municipalities consider drawing on their reserves as part of a comprehensive strategy for dealing with a fiscal crisis. But the City's reserves have declined in recent years, and City officials said they are reluctant to tap them now because a further reduction could lower the City's credit rating. This could make it more expensive for the City to borrow funds for street improvements and other capital needs. One of the major bond rating agencies recently downgraded the City's credit rating because of the revenue shortfall.

An October 2019 BGR report on City budget trends shows that one reason for the declining reserves is that the City strayed from fiscal best practices by using one-time revenues to cover recurring expenses. For example, the City used a \$33 million upfront payment for the 99-year lease of the former World Trade Center it received in 2018 to pay for raises for police officers. This covered the cost of the raises for two years until, as projected at that time, recurring revenues would grow to absorb the costs. Government finance experts advise using such one-time revenues on nonrecurring expenditures, such as capital improvements, or to bolster reserve funds. If the City had found another way to pay for the police raises or had phased them in as recurring revenues permitted, it could have placed the \$33 million in its reserve fund.

As shown in the chart, the City had a negative fund balance as recently as 2012. During the next three years, the City added substantially to its reserves, improving its financial security and credit rating. The subsequent drop off in reserves has put this progress at risk. The City projected to end 2019 with \$55 million in reserves. This is below its reserve target of 10% of recurring revenues, or \$69 million, based on the current budget. It is also far below the 17% target that government finance experts recommend for general funds, or \$111 million.

CITY OF NEW ORLEANS YEAR-END GENERAL FUND RESERVES COMPARED TO THE CITY'S TARGET LEVEL, 2010 TO 2019

(\$ in millions, unadjusted for inflation)



*projected

BGR analysis of City of New Orleans historical year-end fund balances, 2010-2018, and projected fund balances 2019-2021, as presented to the Revenue Estimating Conference in August 2019.

The need to rebuild the City's General Fund reserves for long-term budget stability should be a key focus of policymakers and citizens after they address the immediate fiscal fallout from the pandemic. The long-term goal should be to reduce reliance on one-time or non-recurring revenues to cover General Fund expenditures. As BGR recommended in [A Look Back to Plan Ahead: Analyzing Past New Orleans Budgets to Guide Funding Priorities](#), the City should create a long-term financial plan to identify revenue sources, forecast expenditures and set funding priorities. Efforts to cut costs or slow their growth should be comprehensive and systematic. This should be a highly collaborative process that involves elected officials, staff and the public. Officials should clearly communicate the plan's objectives and the strategy for achieving them. It is also important to update the plan periodically to account for changes in needs and financial circumstances.

To deal with the more immediate consequences of the deficit, BGR's report can help policymakers identify potential cost-cutting options. While the City achieved substantial savings in certain areas during the past decade, including costs for sanitation and General Fund debt service, most other departments experienced increases. Overall, inflation-adjusted General Fund expenditures grew from \$575 million to \$702 million in 2019, a 22% increase.

To track City spending, the report includes a listing of General Fund expenditures for more than 30 departments and other line items from 2010 to 2019. The report

then analyzes the change in dollars and percentages over the decade for each budget area. The report urges City leaders to evaluate the factors driving the growth in each category and assess whether the expenditures are appropriate. They should focus first on areas with the highest growth both in terms of dollars and percentage increases. Click below to access an updated list of General Fund expenditures that includes the adopted 2020 budget.

See Changes in General Fund Expenditures, 2011 to 2020

Department and line-item expenditures that BGR identified as warranting further scrutiny included the following:

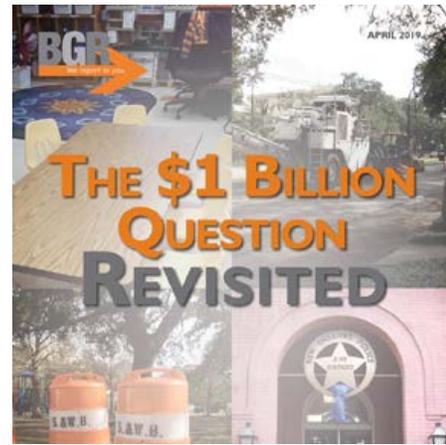
- **Parking and traffic camera enforcement.** Costs for parking and traffic enforcement have grown rapidly, as shown on [pages 28-29 of the BGR report](#). If the costs had remained proportional to revenues the City receives from adding traffic cameras and increasing parking meter rates, the City would have an additional \$11 million annually. The City should review its contracts for these enforcement costs to identify potential savings.
- **Clerk of Criminal District Court.** The City must provide the Clerk of Criminal District Court nearly \$4 million a year largely as a result of Orleans Parish's fragmented court system, as discussed on [pages 33-34 of the report](#). In other parishes that do not have separate criminal and civil courts, filing fees for civil cases help cover the cost of handling criminal cases. Noting that the Clerk of Civil District Court runs sizable annual surpluses, the BGR report says policymakers should consider a potential revenue-sharing arrangement to defray some or all of the City's funding for the Clerk of Criminal District Court.
- **Funding for the mayor's office and mayoral initiatives.** Inflation-adjusted expenses in this category more than doubled to \$14.2 million during the past decade, as noted on [pages 30-32 of the report](#). This increase was largely driven by the creation of six special offices to focus on specific issues or initiatives. BGR called on the City, which now has a dozen such offices, to review them to identify potential efficiencies. In the months ahead, a review of the special offices would also provide an opportunity to optimize the structure of mayoral offices for post-crisis City governance.

Difficult decisions lay ahead as City leaders assess how to deploy revenues optimally during the economic downturn – and beyond. The magnitude of this unprecedented challenge calls for decisive action grounded in careful analysis. BGR offers its *A Look Back to Plan Ahead* report to assist the City in its effort to identify prudent options to adjust its budget in response to the crisis.

Committee Proposes Revenue-Generating Options after Completing Study as BGR Recommended

A New Orleans City Council committee released

a [report](#) before the onset of the public health crisis that makes recommendations for increasing revenue for essential public services and infrastructure. The [Ad Valorem & Dedicated Revenue Special Committee](#) reviewed tax dedications and other revenue-generating options to identify ways to increase funding for high-priority needs. The report notes that BGR called for such a review in a series of reports in recent years that presented a comprehensive analysis of the use of tax revenues in Orleans Parish.



BGR began that analysis with its 2015 report, [The \\$1 Billion Question: Do the Tax Dedications in New Orleans Make Sense?](#) In April 2019, BGR updated this analysis in [The \\$1 Billion Question Revisited](#), to account for the growth in local tax revenues from \$1 billion to \$1.25 billion parishwide. During the four-year period, BGR found that the City took steps to fund critical needs primarily through new taxes and growth in General Fund revenues, rather than through the rededication of existing taxes. BGR restated its core recommendation from 2015 by calling for a reevaluation of local tax dedications in Orleans Parish to identify opportunities for redirecting revenue to fund necessary improvements to infrastructure and public services.

The City Council formed its special committee in July 2019 to take a deeper look. BGR presented its research findings on tax dedications at the initial hearing, and it recapped other research reports on nonprofit property tax exemptions at a subsequent hearing. The committee's February 2020 report makes several recommendations. BGR has not taken a position on any of them at this time, but summarizes them here for information only:

Restructure and Consolidate Property Taxes. The City has four property taxes that will expire next year unless voters renew them. The taxes originally totaled 10.9 mills, but the City currently levies them at a rolled-back rate of 5.82 mills. The taxes are dedicated to libraries, capital improvements, housing, economic development, streets and traffic signals. As the millages come up for renewal this fall, the committee called on City administrators to consider consolidating some of them, particularly the ones dedicated to infrastructure, to allow greater flexibility and efficiency in their use. The committee also urged the administration to review whether the current dedications are aligned with the City's needs and propose changes as warranted.

CITY OF NEW ORLEANS PROPERTY TAXES SET TO EXPIRE IN 2021

Millage	Original rate	Current rolled-back rate
New Orleans Public Library	4 mills	2.58 mills
Streets and traffic signals	1.9 mills	1.77 mills
Housing and economic development	2.5 mills	0.91 mills*
Capital improvements and infrastructure	2.5 mills	0.56 mills
TOTAL	10.9 mills	5.82 mills

*The current budget allocates the entire millage for housing.

Parcel Fee for Tax-Exempt Nonprofit-Owned Properties. The committee received information from BGR about how Louisiana provides an [overly broad tax exemption](#) to nonprofit-owned properties when compared to national norms. BGR also discussed its recommendations for the Legislature to tighten eligibility requirements and improve administration. Other speakers, skeptical of the Legislature's willingness to pursue those changes, suggested instead that the council consider ways to raise revenue from nonprofits. The report recommends that the City Council craft a ballot proposition to impose a parcel fee on tax-exempt nonprofit-owned properties. A council-appointed task force began studying the issue in January.

Verify Property Tax Exemptions. The report indicates that some properties with expired Industrial Tax Exemptions mistakenly remained exempt from taxation, costing taxing entities nearly \$1 million annually. It recommends that the council consider implementing oversight measures to prevent this from happening. The report also calls for the council to move forward with an audit program to identify properties with duplicate homestead exemptions.

Rededicate Slot Machine Taxes. The State dedicates about \$6.6 million from its slot machine taxes in Orleans Parish to various entities. According to the report, the Louisiana Stadium & Exposition District receives \$2.7 million to fund contractual obligations to the New Orleans Saints and New Orleans Pelicans. Another \$1.9 million goes to the New Orleans City Park Improvement Association. The Greater New Orleans Sports Foundation, a nonprofit organization that seeks to draw sporting events to the New Orleans area, is set to receive \$1 million. Six other entities will receive a total of \$949,000. The report calls for the City Council to review whether these dedications represent the community's most pressing needs and pursue changes as necessary through the Legislature.

Rededicate Surplus Funds. The committee found that the City has 56 special funds that contain a total of \$46 million for specific purposes. This includes \$8.4 million for capital improvements, \$7.5 million for housing and \$2.7 million for economic development. The report indicates the City Council and administration will review potential rededications of some of these revenues. The report noted that any changes in the use of dedicated tax revenues would require voter approval.

Review the Wisner Trust. In 1914, philanthropist Edward Wisner donated more than 50,000 acres of land, including a sizable portion that supports oil importing operations in Port Fourchon, in a trust to the City. Proceeds from leasing the land are divided among various entities and heirs, with the City receiving a 34.8% share. The report indicates the 100-year trust expired in 2014, at which time the City was to receive ownership of the land. However, a trust advisory committee continues to manage the properties and distribute lease proceeds in accordance with the trust. The report calls for prioritizing a review to identify potential increased revenue for the City.

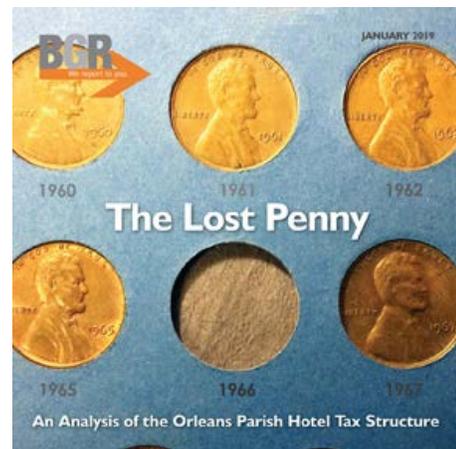
Increase efficiency. The report urged the administration to continue its efforts to systematically review City agencies to minimize duplication and increase efficiency. The review is part of the zero-based budgeting process that the City piloted with the 2020 budget. In zero-based budgeting, all budget line items start at zero and every proposed expenditure must be justified. The focus is not on what to cut but rather on what to keep. The approach is intended to go beyond making incremental changes to the prior year's budget and put all funding under scrutiny.

PROGRESS UPDATE

An update on implementation of recommendations from past BGR reports

Restoring the Lost Penny

In January 2019, BGR released [*The Lost Penny: An Analysis of the Orleans Parish Hotel Tax Structure*](#), which presented a comprehensive picture of where \$200 million in hotel tax dollars are going in Orleans Parish. The report focused primarily on the share for the City of New Orleans, which had a 1% hotel tax suspended by state law for more than 50 years. This “lost penny” of hotel tax deprived the City of \$12.3 million a year that it could have used to address pressing needs. The report called for the Legislature to restore the suspended tax to bring the parish’s hotel tax



structure more in line with best practices for taxation as well as state and national norms. The Legislature did so effective July 1, 2019, as part of an infrastructure funding package for the City and the Sewerage and Water Board of New Orleans. While the pandemic-related downturn in hotel activity has decreased this year's revenue projections, the hotel tax will support infrastructure work for years to come. The Legislature also codified into state law the 15 separate acts governing the New Orleans Ernest N. Morial Convention Center as the report recommended to improve transparency.

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