



NORFOLK

Office of the City Manager

April 16, 2013

**Honorable Mayor and City Council
City of Norfolk, Virginia**

I respectfully submit to you the Proposed Fiscal Year 2014 financial plan for the City of Norfolk, which is comprised of the Operating, Internal Service Fund, Enterprise Fund, Special Revenue Fund, Capital Budget, and Annual Plan for the Housing and Urban Development Block Grant programs. A summary of the Proposed Financial Plan is shown in the table below.

Fiscal Year (FY) 2014 Financial Plan	
Fund	Proposed Budget
General Fund	\$811,504,726
Enterprise Funds	\$130,992,500
Special Revenue Funds	\$60,875,771
Internal Service Fund	\$13,655,900
Total Operating Funds	\$1,017,028,897
Healthcare Fund	\$57,931,973
Total Operating with Healthcare Fund	\$1,074,960,870
Capital Improvement Plan	\$127,290,582
Total Operating and Capital Funds	\$1,202,251,452
Annual Plan for HUD Block Grants	\$5,678,928
Total Financial Plan	\$1,207,930,380

The Proposed General Fund budget is \$811.5 million. The total General Fund budget increase is \$11.7 million or a 1.5 percent increase from the Approved FY 2013 Budget. As in recent years, the Proposed FY 2014 Budget continues efforts to streamline government and contain costs as we find our footing during this time of economic uncertainty. Therefore, the budget I present to you today does not contain “bells and whistles” but mainly provides the resources needed to continue services as we know them today.

During the last three years, the city has made difficult but necessary decisions through the economic downturn. However, as we enter another year of tough economic times, the

avenues available to minimize revenue loss are becoming scarce. It will be increasingly difficult to find savings in the future since we have already reviewed existing operations and implemented efficiencies, reduced current programs, deferred projects, and delayed necessary infrastructure repairs that may increase costs in the future. We are committed to streamlining government and employing best practices, but our current needs and service levels exceed our available resources.

While I am presenting to you a balanced budget, it should not be mistaken for a *structurally balanced* budget. A *structurally balanced* budget matches ongoing expenditures with ongoing revenues. The Proposed FY 2014 Budget development process included making tough choices and used one-time revenues for ongoing expenses to preserve our current level of service. Additionally, the Proposed Budget maintains service levels that were decided on last year, which included restorations that opened libraries on Mondays and expanded pool hours at recreation centers.

With the various tradeoffs made during the budget development process, the Proposed FY 2014 Budget continues our goal of being a well-managed government and is highlighted by the following:

- Provides a two percent salary increase for city employees effective January 2014
- Increases the Real Estate Tax Rate by two cents from \$1.11 to \$1.13 and dedicates all revenues from the increase to the new School Construction, Technology, and Infrastructure (CTI) Program
- Provides a strategy to fully fund Norfolk Public Schools (NPS) FY 2014 budget request
- Continues to realign, reallocate, and refocus resources in support of the six priority areas with an emphasis on two priorities; Lifelong Learning, and Economic Vitality and Workforce Development
- Accelerates the design and construction of two fire stations
- Implements a city-administered healthcare plan resulting in significant savings for the city, NPS, and Norfolk Redevelopment and House Authority
- Decentralizes central Storehouse operations
- Consolidates Communications and Public Information with Information Technology to form the new Department of Communications and Technology, reducing operating redundancies
- Continues IMPACT to improve customer service
- Continues implementation of “Smart Processing” and increases Planning fees to support needed technology improvements
- Increases Ambulance fees to support the cost increase for time critical emergency response and effective patient care
- Increases Police Record Service Fees for Fingerprinting, Accident Reports, Incident Reports and Criminal Records to help offset the expenses associated with providing these services.

GUIDING PRINCIPLES

The Proposed FY 2014 Operating and Capital Improvement Budgets continue efforts launched in February 2011 to become a well-managed government. Throughout the budget development process, the following principles have been employed to achieve results: we reinvested existing resources to fund the city's highest priorities; engaged employees and residents in the budget development process; identified further opportunities for operating efficiencies through internal and external collaboration; eliminated redundant processes and trimmed excess from the budget; increased employee productivity throughout the organization; and continued to focus on cost containment measures. These principles continue to support the efforts undertaken by City Council over the past three years.

Uneven economic recovery, stagnant revenue collections, and rising costs of providing services have required us to focus on additional cost containment strategies to maintain the level of service Council approved in FY 2013. These additional strategies are needed to address cost increases that are outside of our control, such as state and federal mandates, inflation, and rising energy and utility costs. The changing healthcare landscape, the increasing cost of retirement and debt service, and the opening of new facilities are challenges we will continue to face in the future.

These guiding principles outlined above will continue throughout FY 2014 to increase overall performance. However, as we continue to examine opportunities to reduce costs, we must also move towards building a *structurally balanced* budget to secure and improve the financial position of the city.

BUDGETING BASED ON PRIORITIES

As you may recall, together we undertook a priority setting process. The Proposed FY 2014 Budget is built around those six City Council priorities:

- Accessibility, Mobility and Connectivity
- Economic Vitality and Workforce Development
- Environmental Sustainability
- Lifelong Learning
- Safe, Healthy and Inclusive Communities
- Well-Managed Government

While work continues on all six priorities, this year's Proposed Budget focuses on two priority areas; **Lifelong Learning**, and **Economic Vitality and Workforce Development**. All city departments were instructed during this year's budget development process to focus on these two priorities.

FINANCIAL BACKDROP

Although the 'Great Recession' officially ended in June 2009, the recovery has been uneven across sectors of the economy. State governments, which rely on income and sales taxes, have improved with the growth in jobs and recovery of consumer spending. Local governments, which are heavily reliant on property taxes, have lagged and been held back by the slow recovery of the housing market. The recent uptick in the regional and local housing markets is encouraging. In Norfolk, the median and average sales price of homes sold in 2012 rose by 5.1 percent, the first annual increase since 2007. However, distressed homes, which are typically sold at a discount, continue to make up a significant portion of homes for sale in the region. While the housing market is beginning to stabilize, the recovery is still slow and inconsistent.



Jobs in the region continued to grow in 2012 but remained below pre-recession levels. Additionally, the recovery may be set back by the impact of Sequestration. According to Moody's Investors Service (Moody's), Virginia is at the top of the list of states expected to be impacted by Sequestration due to the high concentration of defense procurement spending in the state. Consequently, Moody's assigned Virginia a negative outlook. Since defense spending makes up

nearly 46 percent of our regional economy, Hampton Roads and Norfolk are likely to be impacted by Sequestration.

While the impacts are unknown at this time, Sequestration could directly impact Norfolk through the loss of funding from various federal programs such as the Department of Housing and Urban Development's Community Development Block Grant Program, the Department of Education's Impact Aid, and the Department of Labor's Workforce Investment Act state grants.

STRUCTURAL BALANCE

What does it mean to have a structurally balanced budget? Simply said, structural balance exists when ongoing expenses are tied to recurring revenue sources. When I arrived in Norfolk in 2004, the budget document that year outlined issues relating to the structural imbalance of \$26 million between revenues and expenditures. Many of the issues that led to the imbalance then are the same ones we face today including: a slowdown of national economic recovery; the continued escalation for the cost of goods and services; increased cost of healthcare and the city's retirement system; the continued reduction of state funding to the city; and the accumulation of previously deferred maintenance and replacement of critical infrastructure.

A structurally balanced budget is one mechanism to combat the cyclical effects of these types of financial issues. Additionally, the factors that support a structurally balanced budget are used in determining the fiscal health of the city and credit rating agencies use it to grade Norfolk in the bond market. We believe structural balance can be achieved within the next five years. To do this, we need to implement a combination of revenue and expenditure actions.

We must be practical in our spending, make ongoing and sustainable reductions, and find new cost efficient ways of providing services. Additionally, we must have greater flexibility in raising revenue.

As part of our effort to be a well-managed government, the establishment and maintenance of general operating reserves is considered one of the most effective management practices a local government can employ. Reserves help to cushion against annual cash flow disruptions. Specifically during FY 2012, we allocated \$773,328 of the FY 2011 surplus to raise the unassigned General Fund balance to \$42 million to further strengthen reserves. As a result, the unassigned General Fund balance currently exceeds five percent of the budget with the aspiration to increase this goal over the next decade. Additionally, the city has increased the Risk Management as well as the Economic Downturn/Leveling Reserves. The Risk Management Reserve was enhanced in FY 2010 and FY 2012 to \$3 million and we allocated \$1 million of the FY 2011 surplus to the Economic Downturn/Leveling Reserve, for a total of \$3 million.

The decline in revenue from major revenue sources since the start of the Great Recession resulted in the city increasing its reliance on carryforward funds to balance the budget. As real estate assessments declined, the use of carryforward funds increased significantly in FY 2012 and FY 2013, accounting for at least two percent (\$16-\$19 million) of the Approved Budget. Without the carryforward, the budget would have needed to remain flat even though the city still faced rising operating costs.

The carryforwards and actions to realign, reallocate, and refocus resources enabled the city to provide a balanced budget in FY 2013. This balanced budget was accomplished without raising taxes or reducing service levels, and with minimal reductions in staff. However, the ability to maintain service levels without a full recovery in real estate valuations is not sustainable.

WHAT HAS BEEN DONE TO ADDRESS THE IMBALANCE?

Throughout FY 2013, we worked to forge partnerships that would leverage existing resources to increase efficiencies. One of the major initiatives undertaken in FY 2013 regarding shared services involved the Hampton Roads Partnership and their efforts to bring the cities of Norfolk, Chesapeake, and Virginia Beach together to identify at least 13 service sharing opportunities across jurisdictional lines. The first three of these initiatives are:

- Sign Shop Services - Manufacturing of standard traffic control signs for the three cities that will save Norfolk approximately \$15,000 per year, as well as increase efficiency of sign installation and repair services through an agreement signed between the three cities. Virginia Beach has taken the lead to oversee sign production.
- Elevator Inspections - Norfolk is reviewing Chesapeake's processes for contracting out elevator inspections. The new model could result in the cities sharing third party



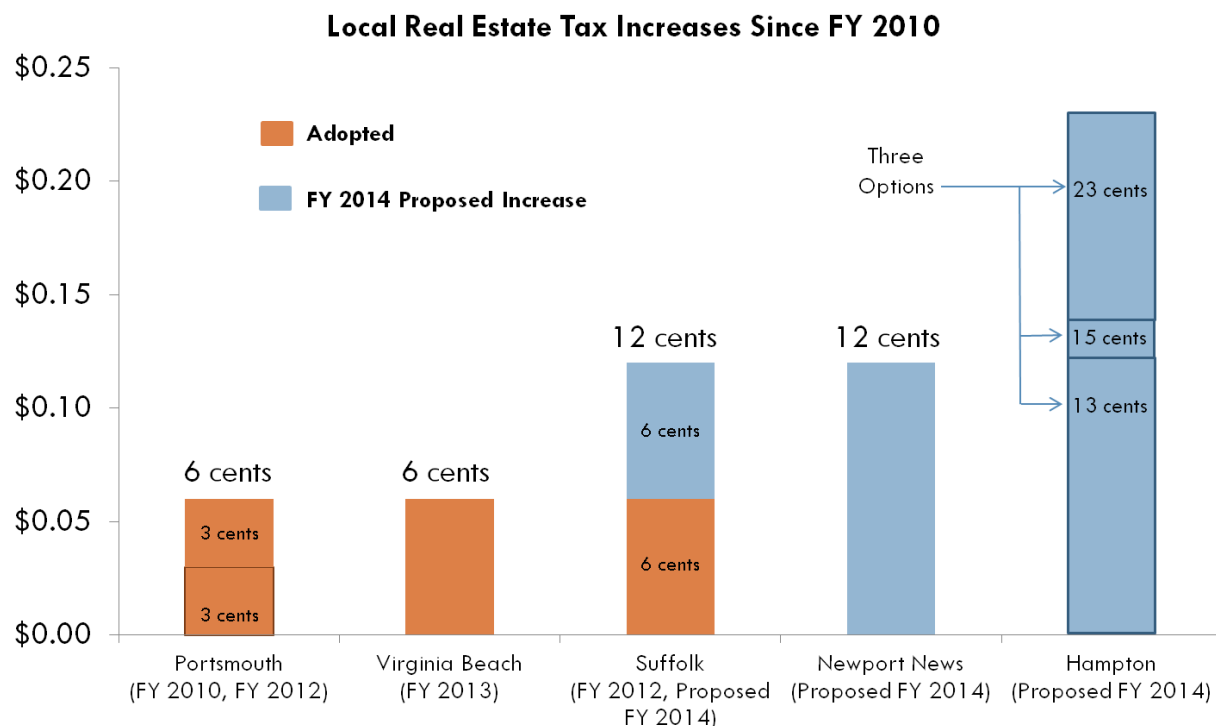
inspectors for the inspection of elevators in public and private buildings.

- **Permitting Services** - The three cities are working collaboratively on standardizing permitting processes beginning with the use of common forms for various building permit applications. A long-range goal is to provide the public access to an online permitting process through a shared internet portal.

Sharing services also encourages work across traditional organizational structures by removing silos to create operating efficiencies. Additionally, the benefits of these types of agreements have led the city to move forward with: developing a joint grass cutting initiative on public property with Norfolk Redevelopment and Housing Authority (NRHA); internally decentralizing its central Storehouse operations; and working to strengthen the Norfolk Healthcare Consortium. The joint grass cutting initiative with NRHA will promote citywide beautification efforts, improve efficiencies by reducing mobilization costs and allow for the clustering of properties for grass cutting in specific areas of the city. Some of these initiatives are further detailed under the “Efficiency and Effectiveness” section of this message.

HOW HAVE NEIGHBORING LOCALITIES ADDRESSED BUDGET IMBALANCES?

The city’s path to a balanced budget in the period of declining revenues has been markedly different than the path chosen by most of our neighbors. The cities of Portsmouth, Suffolk, and Virginia Beach have addressed their budget imbalance by raising taxes. Since FY 2010, these three cities have increased their real estate tax rate as identified in the following chart.



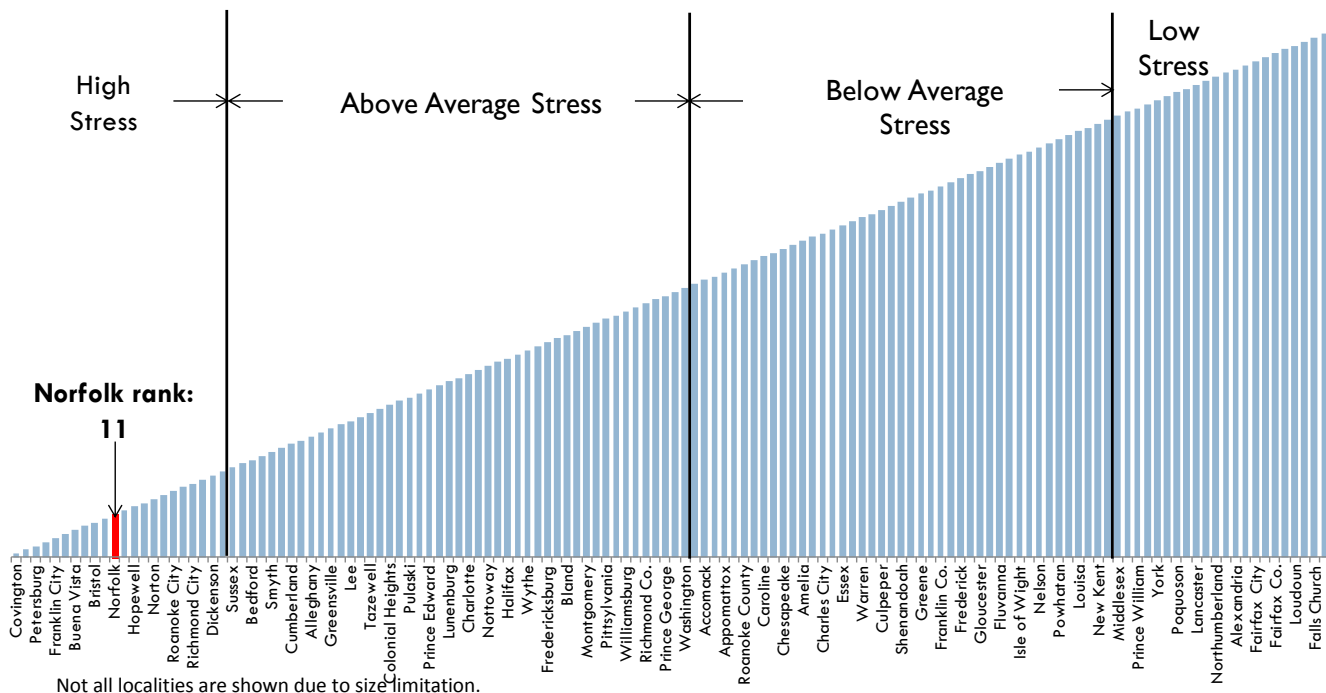
Our continued dependence on carryforwards and the desire to maintain the current service levels in the long-term requires the city, like other Hampton Roads communities, to increase revenues by way of real estate tax increases. While it has been three years since the first Hampton Roads city began increasing real estate taxes, we have maintained the same tax rate as prior to the recession; however, the increasing fiscal stress presents challenges in our available options.

FISCAL STRESS

Norfolk is identified in the Commission on Local Government's most recent report as the 11th most fiscally stressed community out of 134 localities in the Commonwealth. The fiscal stress index is a measure of a locality's overall fiscal well being relative to other localities in Virginia. The fiscal stress index is comprised of three components:

- Revenue capacity per capita (the potential ability of a locality to raise revenue)
- Revenue effort (the extent to which a locality has used its revenue capacity)
- Median household income

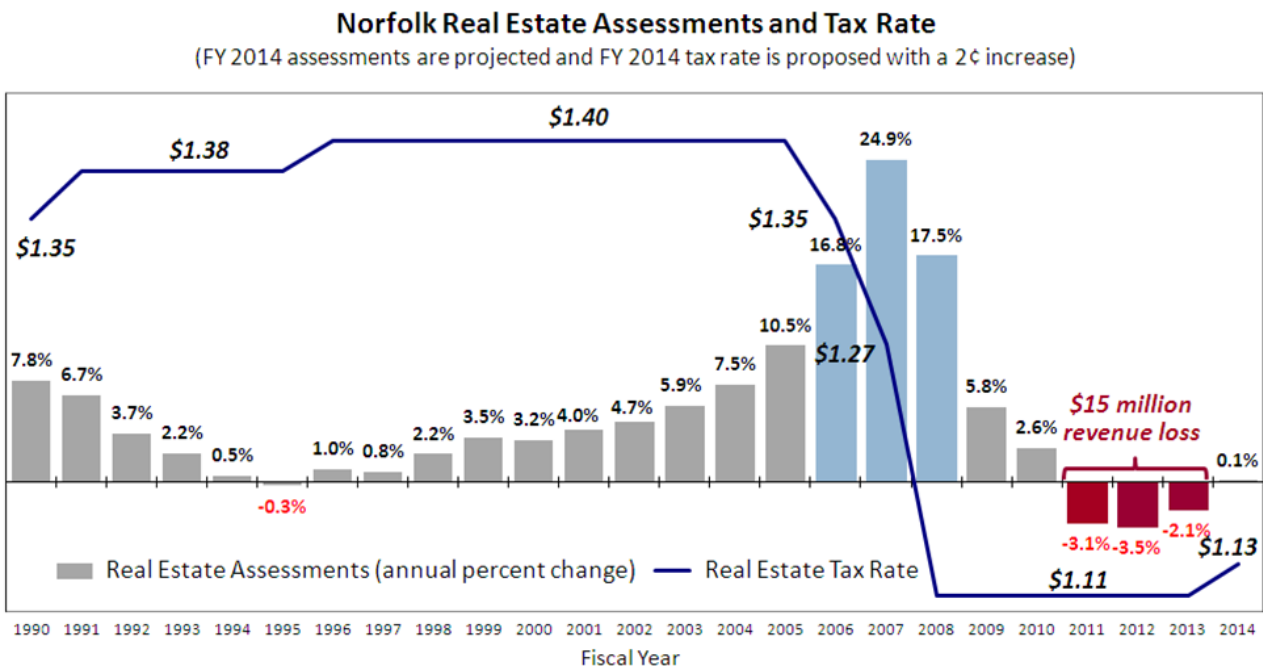
The chart below provides a comparison of Norfolk's fiscal stress index in relation to other localities across the state.



REVENUE PICTURE

Real estate tax revenue is the largest locally-generated revenue source and makes up a quarter of the city's General Fund revenue. In the past three years, real estate assessments have declined and as a result, the city has lost an estimated \$15 million in real estate tax revenue. This is no small loss. **Assessments would have had to grow by about eight percent (or an increase of nine cents on the tax rate) to get back to the same level as FY 2010.**

In FY 2014, overall real estate assessments are projected to increase by approximately 0.11 percent based on a preliminary estimate from the Real Estate Assessor's Office. However, this increase does not apply to all homeowners. Residential assessments (including condominiums) are projected to decline again for the fourth consecutive year in FY 2014, by about one percent. This means that of the 272 neighborhoods, only 66 neighborhoods, or one in four, will see an increase in assessed value.



The last time the city raised the real estate tax rate was in FY 1996, when the tax rate went from \$1.38 to \$1.40. Since that time, as real estate assessments soared from 2003 to its peak in 2010, the city reduced the tax rate by 29 cents over a three year period, from \$1.40 to \$1.11. The Proposed Budget includes a two-cent increase in the real estate tax rate from \$1.11 to \$1.13. The revenue from the tax increase will be dedicated entirely to NPS to create the Construction, Technology, and Infrastructure (CTI) program. The CTI is further detailed under the "Lifelong Learning" section of this message.

If residential assessments did not change from last year, a two-cent increase would have cost the average homeowner about \$40 per year. But because of the projected decline in residential assessments in FY 2014, the average homeowner's tax bill will only increase by

about \$13, from \$2,258 to \$2,271 with the two-cent increase. Moreover, the average homeowner, with the two-cent increase, will still be paying about \$304 less than they were in FY 2010, when residential assessments were at their peak. The average homeowner in one in five neighborhoods will see no increase in their tax bill.

Impact of FY 2014 Proposed 2¢ Increase in the Real Estate Tax Rate	
FY 2013: Average homeowner's tax bill (at \$1.11 rate)	\$2,258
Increase in average homeowner's bill if rate increases by 2¢	\$40
FY 2014: Average homeowner's tax bill (at \$1.11 rate)	\$2,230
Average savings from decline in residential assessments	-\$27
FY 2014 Proposed: Average homeowner's tax bill (at \$1.13 rate, 2¢ increase)	\$2,271
Difference from average homeowner's tax bill in FY 2013	\$13
Difference from average homeowner's tax bill in FY 2010 of \$2,575	-\$304

Note: Amounts may not sum due to rounding.

Aside from real estate, other local taxes are projected to hold steady. However, these revenues are sensitive to changes in economic activity. The uncertainty of Sequestration and the end of the payroll tax holiday may negatively impact this revenue. These revenue sources make up about 19 percent of General Fund revenue and include various taxes such as, sales, business license, hotel and motel, restaurant, and recordation taxes. Overall, these local taxes began to rise in FY 2011 after declining for two straight years and have been gradually approaching pre-recession levels.

Revenues from the Commonwealth are expected to increase by about \$2.6 million to nearly \$292 million in FY 2014. This projected increase is largely due to the restoration of the flexible reduction in aid to localities, which was first imposed in the FY 2009 budget. However, state revenues are still below pre-recession levels and not all the reductions from the Commonwealth have been restored. Five years ago, revenues from the Commonwealth made up about 41 percent of the FY 2009 General Fund budget; in FY 2014, these sources make up 36 percent of General Fund budget, a loss of \$46 million.

USER FEE INCREASES

In addition to the proposed two-cent increase to the real property tax rate, I am proposing user fee increases in four areas in response to the rising costs to provide services. User fee increases are proposed for various Norfolk-Fire Ambulance fees, Police Record fees, Planning fees, and Parking fees. The increasing cost of delivering these services has resulted in a proposed fee increase to recoup a greater percent of the actual cost for services provided.



User fee increases are proposed for Norfolk's Fire-Rescue fees for ambulance services. Periodically, the city reviews the rate structure with its emergency medical services billing provider to ensure that the city is achieving the maximum insurance funding for these services. Based on the most recent review, it is recommended that the city increase these rates.



Police Record Service Fee increases are also proposed for Fingerprinting, Accident Reports, Incident Reports and Criminal Records to help offset the expenses associated with providing them. After researching the user fees of other cities, it has been determined the City of Norfolk's user fees are relatively low in comparison and do not cover the cost of production. The Police Record Service fees will be increased to \$10.00 to help offset the expenses associated with providing them. The change in fee structure for record services is projected to increase revenue by almost \$100,000 per year.

Planning user fee increases are proposed to be reinvested back into our "Smart Processing" initiatives for technology improvements. Smart Processing is a philosophy promoting exceptional customer service by ensuring businesses and homeowners have a seamless experience while going through the city's development process.



The city's Parking System, which consists of more than 20,400 spaces, including 15 garages, nine lots and over 700 parking meters, has been a cornerstone for Downtown revitalization and economic vitality over the last 15 years. The Parking System's expenses are covered solely through the user fees of the self-supporting Parking Enterprise Fund. User fee rate adjustments, which were last implemented in 2009, have not kept pace with inflation, while expenses continue to escalate. To maintain fiscal stability, the Proposed Budget recommends several financial and operational changes, including some user fee rate adjustments. The proposal:

- Increases transient or short-term parking rates, except at MacArthur Center
- Increases parking meter rates in Downtown and around Old Dominion University
- Increases fines for parking violations
- Expands automation in the parking garages
- Institutes annual rate adjustments beginning in 2017 for transient, meter, and violation prices that are tied to the rate of inflation

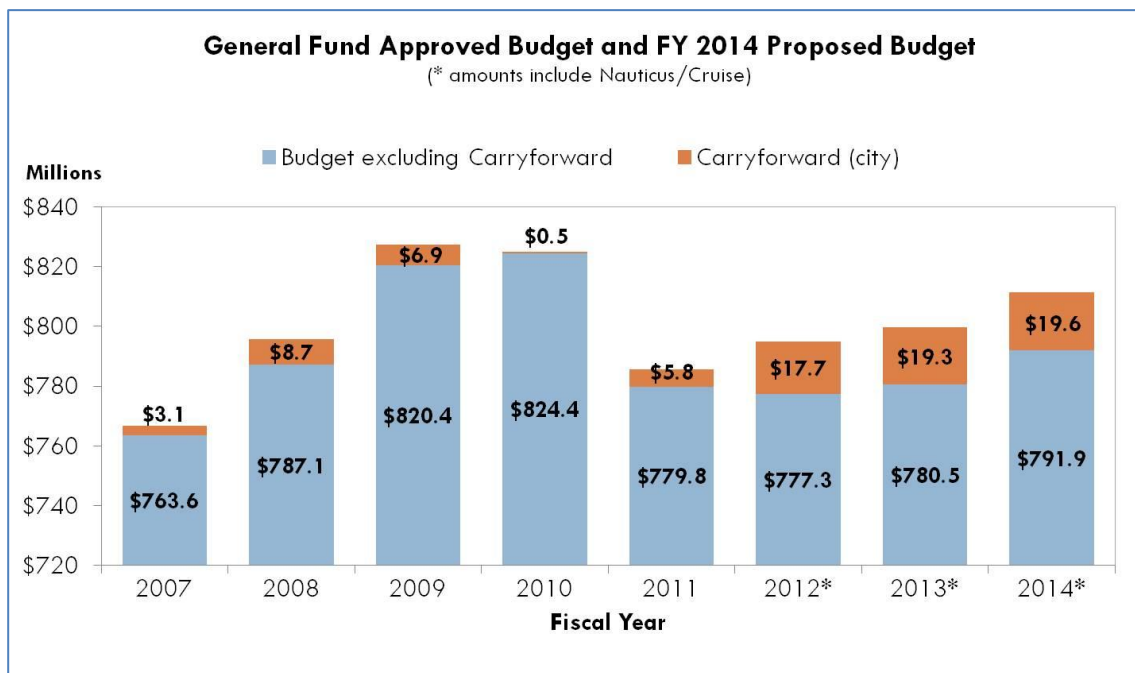


It should be noted that the expansion of automation in parking garages is a parking industry best practice. This practice optimizes operations through the use of technology. It is anticipated that fully automated lanes will go into effect at the beginning of calendar year 2014.

There are no user fee rate adjustments proposed for monthly parking, which also includes residential parkers. Additionally, no proposed user fee rate adjustment is recommended for recreational rates.

EXPENDITURE CHALLENGES – OPERATING BUDGET

Revenue losses over the last three years have significantly impacted the city's ability to operate at identified service levels. Operating costs are significantly impacted in the Proposed FY 2014 Budget by healthcare, retirement, inflation, and increases in energy. To address the expenditure challenges, it was our goal throughout the budget development process to begin the groundwork for a more structurally balanced budget in order to further strengthen the city's fiscal health. However, at this point in time, to meet existing expenditure challenges and to minimize layoffs, the city's reliance on carryforwards to support operations will continue.



A major cost driver in the Proposed Budget is the city's contribution to the Norfolk Employees Retirement System (NERS). Two actions in FY 2013 have had significant impacts on the Proposed Budget. Last year, the Approved FY 2013 Budget provided a two percent cost of living adjustment (COLA) for retirees. This COLA increased annual retirement payout costs by approximately \$1.4 million. While we would like to provide our retirees a COLA it is not factored into the base calculations. The Retirement Board has indicated that should we provide COLAs regularly it would become a standard practice versus an ad hoc one. Once it becomes a standard practice, it will have a significant impact on the city's contribution formula for retirement. A second action impacting retirement costs was the transition of the Norfolk Community Services Board (NCSB) into the city's structure. Bringing NCSB employees into the city's retirement system also contributed to the increase of the FY 2014 retirement costs.

Similar to retirement costs, healthcare costs are a significant component of the budget. The city is a member of the Norfolk Healthcare Consortium (Consortium), along with NPS and the NRHA. The Consortium has worked to employ best practices to keep costs below the national and regional average. Even with these efforts, healthcare premiums have increased 6.4 and 7.7 percent over the last two plan years respectively. In December, the Consortium's healthcare consultant projected a 15.2 percent premium increase beginning in January 2014.

The increase is due to both an annual healthcare cost increase assumption, and the beginning of the Affordable Care Act in 2014. To control costs and limit the impact on the city and our employees, the Proposed FY 2014 Budget includes the transition to a city-administered healthcare model effective January 2014. The proposed model is similar to what most Hampton Roads cities currently use. The transition, which is projected to save the city and our employees \$2.5 million in FY 2014, is further detailed under the "Efficiency and Effectiveness" section of this message.

Even with the significant challenges facing the city, there are opportunities to proactively develop strategies in the short and long-term to improve the city's financial position. Short-term strategies include:

- Re-evaluate the effectiveness of programs and services that receive General Fund subsidies;
- Strengthen Internal Service Funds and Enterprise Funds to ensure they are self-supporting; and
- Engage citizens in conversations about the expected levels of services and what we can really afford to fund.

Long-term strategies include:

- Reduce the use of one-time revenues to fund ongoing operating costs for a more structurally balanced budget;
- Reduce the use of year-end budget surpluses to fund ongoing operations;
- Temper the use of bond financing and decrease the city's debt burden; and
- Increase the reserves to help address shortfalls and potential costs of catastrophic events.

EFFICIENCY AND EFFECTIVENESS

During the economic downturn, the city began new efficiency initiatives to continue providing quality programs and services to Norfolk's residents, businesses, and visitors. Strategic realignment, benchmarking performance measurement, budgeting to priorities, and service sharing agreements are now integrated into city operations as part of being a well-managed government.

During the FY 2013 budget development process, the city identified strategic initiatives that would enhance operating efficiencies. After last year's budget was approved, we continued our efforts to:

- Collaborate with adjacent cities to create shared services agreements
- Create partnerships with NRHA and NPS to make government operations more efficient
- Closeout accounts that have had no activity for a specified time period
- Re-evaluate aspects of how we manage our debt to better utilize funds and ensure the lowest possible borrowing costs are achieved
- Consolidate departments and services for greater operating efficiencies

The recession has also resulted in all city departments re-evaluating their operations. We are identifying opportunities for operational efficiencies that not only improve productivity but focus on cost containment. In FY 2014, the city will continue efforts to drive down the cost of doing business. Actions proposed include:

- Decentralize central Storehouse operations
- Move the city's Real Estate Division from the Department of General Services to the Department of Development
- Move the city's Purchasing Office from the Department of General Services to the Department of Finance
- Consolidate the Department of Information Technology with the Office of Communications and Public Information to form the new Department of Communications and Technology

Beginning in FY 2014, the central Storehouse will be decentralized and purchases will be procured and monitored by individual departments. The decentralization of the Storehouse is considered an industry-wide best practice that will improve operating efficiencies by promoting just-in-time delivery of goods purchased and reducing the costs associated with maintaining inventories in-house.



In addition to the strategic realignment and reprogramming of resources, the city is exploring ways to combat the rising cost of healthcare. The Consortium, as stated earlier, is focused on providing affordable healthcare for Consortium members. Since its inception, the Consortium has used plan design changes, wellness programs, and most recently, a dependent care audit to stabilize the growth of healthcare costs. The Consortium, as part of the Proposed FY 2014 Budget, will transition to city-administered health insurance beginning January 2014 from a fully insured model. Under the new model, the Consortium will assume the risk and responsibility for the administration and payment of claims rather than paying a private insurance company to assume the risk. A self-insured model allows the Consortium to fully control all aspects of the plan, including setting rates to smooth out the impact of increases on employees. The city-administered healthcare program will be similar to how we already handle risk management.

To do this, the Proposed FY 2014 Budget includes the creation of a Healthcare Fund. The fund will receive revenue from employee, employer, and participating retiree healthcare premiums for all Consortium agencies. These funds will be used to pay medical claims, administrative costs, wellness program costs, and fees related to the Affordable Care Act. Any revenue earned in excess of expenditures will be held as a premium stabilization reserve to mitigate premium increases in future years.

The transition to a city-administered plan is projected to save the city an estimated \$2 million, and save city employees \$567,000 on premiums during calendar year 2014, when compared to projections under the current model. Overall, the transition is projected to save Consortium members, their employees, and participating retirees \$5.3 million in calendar year 2014. No changes are expected in how employees will access healthcare services due to this transition.

Over the last two years, the city has taken on the burden for the majority of healthcare premium cost increases. In both FY 2012 and FY 2013, no cost increases were passed on to employees in the Value Plan despite 6.4 and 7.7 percent premium increases respectively. Employees in the Plus Plan were only passed on half of the premium increases. The city picked up the additional costs in an effort to lessen the burden of the economic downturn on our employees.

Even though the city and its partners have successfully taken steps to limit the premium increase, employees will be asked to contribute their share of the additional 8.2 percent in FY 2014. On average, beginning in Fall 2013, city employees currently enrolled in healthcare will pay an additional \$13.70/month (or 22 percent) towards the average premium increase of \$61.82/month. The city will pick up costs for the remaining 78 percent of the premium increase.

LIFELONG LEARNING

The priority of **Lifelong Learning** ensures residents of all ages are able to reach their full potential, achieve personal goals, and support a prosperous economy through the development of knowledge, skills, abilities, and talents. Lifelong Learning is one of two priority areas that we are focusing on during the upcoming fiscal year.

Norfolk Public Schools

An excellent educational system is an asset to any community. We look forward to continuing to work with NPS as they develop short and long-range plans to improve achievement for all students. NPS has more resources to educate students in the upcoming fiscal year than in FY 2013. The Proposed FY 2014 Operating Budget for NPS is \$307.9 million.

The Commonwealth ties its funding for education to student enrollment. Average Daily Membership (ADM) is the student enrollment count that determines most state funds. As student enrollment declines, so does state support. This is not the case with city funds. Even during difficult times, city support continues to increase. I am proposing to increase local

support by \$6.3 million or 5.9 percent, with \$3.3 million of that being dedicated to the school Construction, Technology, and Infrastructure (CTI) program.

Norfolk Public Schools (NPS) Proposed FY 2014 Budget	
Sources	Proposed Budget
Revenue from the City	\$110,186,600
Revenue from the Commonwealth	\$180,303,062
Revenue from Federal Funds	\$4,545,721
Revenue from Other Funds	\$4,177,226
Carryforwards	\$5,400,000
Subtotal Operating Funds	\$304,612,609
Construction, Technology and Infrastructure (CTI)	\$3,330,000
<i>Total Local support with CTI</i>	<i>\$113,516,600</i>
Total Operating including CTI	\$307,942,609
Grant Revenues and Child Nutrition Funds	\$49,371,032
Total Funds	\$357,313,641
Additional city services contributed to NPS (debt service on school buildings and school buses, school resource officers, school crossing guards, school nurses, grounds and facility maintenance; does not include school construction)	\$16,760,267
Total NPS Budget	\$374,073,908

The Superintendent's Proposed Budget did not request additional funding from the city. The School Board did, resulting in a \$7.3 million request. I recommend addressing this request, in part, through an additional \$3.0 million for the Operating Fund. This \$3.0 million was not easy to find. Because we believe our schools are one of our top priorities, we specifically identified savings within current operations to transfer to NPS.

School Board's FY 2014 request for additional city support/ budget gap	(7,259,673)
Increase city contribution	\$1,000,000
Transfer Public Health School Nurse savings to NPS	\$250,000
One-time funding from city savings initiative (decentralize Storehouse)	\$1,750,000
Total additional city operating support	\$3,000,000

In addition to the \$3.0 million in additional local support, strategies have been identified to close the remaining gap.

Meeting the Remaining Gap	(4,259,673)
Potential Strategies to meet NPS Gap	
Delay salary increase to January 1 st	\$2,100,000
Outsource Custodial Services	\$2,500,000
Total Strategies	\$4,600,000
Remaining Gap	\$0
Potential Surplus	\$340,327

Recommended Strategies:

- NPS delay the proposed two percent salary increases for employees until January 1, 2014. The delay in salary increases will save approximately \$2.1 million, but will still allow the school division to receive approximately \$2.0 million in revenue from the state for the salary increase. This change will also keep the city and school division on par with both city and school employees' receiving salary increases on January 1st.
- NPS analyze outsourcing custodial services to realize savings. According to a proposal it is estimated that NPS can save approximately \$2.5 million by outsourcing its custodial services. The city has outsourced custodial services producing a savings of \$1.0 million annually.

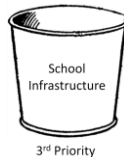
School divisions throughout the Commonwealth are implementing efficiency reviews to find savings that can be redirected to classroom instruction. Suffolk is staggering its school schedule resulting in a savings of approximately \$895,000, and Virginia Beach is implementing a hybrid high school schedule to provide additional opportunities for students that will save at least \$1.1 million. Richmond has an 'Accountability and Efficiency' taskforce. This taskforce recommended \$11.8 million in cost savings strategies for FY 2014, including the closure of two elementary schools.

NPS can also analyze the following items during the upcoming year: align healthcare costs to be more like the city's (currently NPS pays a higher share of costs than the city); realign staff to meet enrollment decline based on Superintendent's Proposed Budget; similar to city practices, phase in additional personnel based on the ability to fill positions; review existing contracts, close out old accounts for projects that are no longer necessary, and implement spending controls; close underutilized schools; and share services with the city for communications, fleet, printing, and purchasing.



School Capital

Over the past decade, the city provided support to construct Norview High, Blair Middle, Coleman Place Elementary, and most recently Crossroads K-8. As you can see, the city has always been committed to building schools. The city has four more schools to building from its original five school commitment. As such, school construction remains a high priority in the FY 2014 Capital Improvement Plan (CIP). The Approved FY 2013 CIP Budget included funds to construct the second and third schools and begin designing the fourth and fifth schools in FY 2016. What **was not** included was funding to begin construction in FY 2017.



The Proposed FY 2014 Budget continues the commitment to build five schools at an accelerated rate. The proposed two-cent real estate tax increase will be dedicated to schools and will fund the school CTI program. With the help of the CTI, the city will be able to fund the design and construction of the next four schools at a faster rate than previously planned. The program will be used solely for one-time capital, technology, and infrastructure improvements for the school division.

The program will be monitored to ensure funding from the tax increase is used solely in support of the CTI. In FY 2014, \$3.3 million will be allocated to the CTI lockbox.

The CTI will (in priority order):

1. Pay the debt service payments for school construction projects
2. Pay for technology to enhance learning within the classroom
3. Provide additional funding to improve infrastructure

The first school, Crossroads K-8, opened in the fall of 2012. As I just mentioned, with the help of the CTI, the Proposed Five-Year CIP includes funds to design and construct the next four schools. In total, the Five-Year CIP includes \$121.0 million in support of school capital projects. In addition to the school construction projects, the Five-Year CIP includes funding to address school major maintenance, to build a field house, to plan for a new Governor's school, and to support the construction of Camp Allen Elementary through a Department of Defense (DoD) federal grant. The DoD is supporting at least 80 percent of the total estimated cost of \$28.7 million on a reimbursement basis. The city's estimated total contribution will be \$5.7 million after the reimbursement.

Proposed FY 2014 Five-Year Capital Improvement Plan (CIP) (in millions)								
Project	Prior Funding	Fiscal Year					Five-Year Plan FY 2014-FY 2018	Total
		2014	2015	2016	2017	2018		
Crossroads (Opened Fall 2012)	\$29.4							\$29.4
Campostella	\$4.7	\$12.3	\$5.0				\$17.3	\$22.0
Broad Creek Area	\$4.7	\$12.3	\$5.0				\$17.3	\$22.0
Larchmont				\$2.2	\$14.8	\$5.0	\$22.0	\$22.0
Ocean View				\$2.2	\$14.8	\$5.0	\$22.0	\$22.0
Subtotal	\$38.9	\$24.6	\$10.0	\$4.4	\$29.6	\$10	\$78.6	\$117.5
Maintenance		\$3.0	\$3.0	\$3.0	\$2.0	\$2.0	\$13.0	\$13.0
Field House		\$0.5					\$0.5	\$0.5
Camp Allen Elementary (20% - city, 80% - federal)		\$4.0	\$17.0	\$7.7			\$28.7	\$28.7
New Governor's school			\$0.3				\$0.3	\$0.3
Grand Total	\$38.9	\$32.1	\$30.3	\$15.1	\$31.6	\$12.0	\$121.0	\$159.9

Five Schools

Note: Amounts may not sum due to rounding.

Public Safety Internship Program

An internal initiative in the Proposed FY 2014 Budget is expansion of internship opportunities in Public Safety for high school and college students. This proposal identifies unique internship opportunities for young men and women interested in careers in Police, Fire or Emergency Communications. The program will promote diversity and retention of qualified candidates for careers in public safety. In partnership with Norfolk State University (NSU) and Tidewater Community College (TCC), the Police Department will work to attract and retain ten qualified college graduates as police recruit candidates. The program will provide the students with opportunities for skill development in the areas of firearms and defensive tactics while still in school. Upon graduation from NSU and TCC, successful interns will be accepted into the Police Academy. A \$10,000 stipend will be provided to eligible candidates over a three year period.

The Department of Fire-Rescue's proposed Public Safety Internship program is structured to identify two qualified Norfolk youths who have an interest in becoming a Norfolk Firefighter. After entering the program, interns will participate in the Academy and upon completion, be offered a full-time Firefighter position.

The Office of Emergency Preparedness and Response (EOC) is working in partnership with Old Dominion University and TCC. The EOC will work to attract and retain one qualified college graduate as a candidate. The program will provide the student with opportunities for skill development in the areas of emergency management and disaster planning.

Urban Youth Summer Academy

The Proposed Budget supports a new community collaborative on the Southside. Regent University is leading a collaborative effort with Southside residents to provide expanded educational opportunities for youth. The 'Urban Youth Summer Academy' is a three week enrichment program for rising sixth graders that is designed to assist them in making a smooth transition to middle school. The program will expose youth to higher education, empowering students toward positive citizenship and community involvement.



Norfolk Emerging Leaders

Support continues for the Norfolk Emerging Leaders (NEL) Program, one of the premier learning opportunities for high school and college students to gain meaningful exposure to careers in public service. The NEL program provides more than 200 high school and college students the opportunity to work side-by-side with experienced municipal employees in a variety of programs and service areas.



Norfolk Youth Leadership Program

The Proposed Budget continues the partnership established last year with NPS to conduct a three day, two night camp with the goal of energizing students with a passion for leadership not just within their schools, but in their communities as well.

ECONOMIC VITALITY AND WORKFORCE DEVELOPMENT

The priority of Economic Vitality and Workforce Development focuses attention and resources on a growing and diversified economy that enhances the quality of life for citizens through a wide range of housing, shopping, educational, cultural, business, and employment opportunities. Norfolk is unique with nearly 37 percent of all property in the city identified as tax exempt (e.g., Naval Base, the Port, universities). To grow the local economy, we are raising the bar on collaboration and customer service. Our vision can be stated simply: Norfolk will create an economic climate that fosters collaboration, innovation, and economic success. We can achieve this objective by creating new and expanding existing partnerships that result in a more focused approach to economic and community development. We will also focus on leveraging resources to achieve common goals with our partners.

Smart Processing

The Department of Development, the Department of Planning and Community Development, and the reconfigured Department of Communications and Technology are working

collaboratively on the Smart Processing initiative. Funding in the amount of \$500,000 has been proposed to promote exceptional customer service by ensuring businesses and homeowners have a seamless experience while going through the city's development process. Over the next year, the city will work to create a 'one-stop' service center for development related permits to help improve processing times, eliminate redundancy and establish an image of certainty and efficiency in the community. Additionally, a streamlined permit process will allow Norfolk to remain competitive and attractive to expanding as well as new business ventures. To this end, the Proposed Budget includes increases to Planning fees that will be reinvested back into the Smart Processing initiatives for technology improvements. These technology improvements will facilitate online submission of plans, enhanced permit tracking and provide for an expedited permitting process.



In addition, to provide our businesses the highest level of services possible in support of reinvestment and new investment into the local economy, this budget proposes instituting concierge services in the Department of Development. The goal of creating a concierge service program is to:



- Provide customized customer care service to foster a business friendly environment
- Focus on collaboration to grow locally owned businesses
- Expand emphasis to support businesses in our neighborhood business districts
- Provide exceptional customer service in business development, permitting, and business retention processes

ACCESSIBILITY, MOBILITY AND CONNECTIVITY



The priority of Accessibility, Mobility and Connectivity focuses attention and resources on instituting a comprehensive system of accessibility options, addressing all traditional transportation modes as well as new technologies, that connect people, goods, and information. The Proposed FY 2014 Budget incorporates programs and activities that improve transportation linkages, connect people and communities, and ensure Norfolk's business services are supported by a reliable technology infrastructure.

Work continues on improving transportation options for Norfolk residents, businesses and visitors. Construction of the Intercity Passenger Rail Facility at Harbor Park is scheduled for completion in September 2013. The 3,500 square foot facility is within walking distance to the Harbor Park Light Rail Station. Additionally, other alternative transportation modes such as bicycling are beginning to take hold. Investments in bicycle infrastructure include improving bicycle roadway safety and increasing the number of secured bicycle parking spaces citywide.

These types of activities are the work of direct collaboration with residents and businesses to make Norfolk a bicycle friendly community.

We are also working to address the backlog of citywide technology projects in the Proposed FY 2014 Budget. These projects include the scheduled laptop replacement for Police and Fire vehicles and the citywide computer and server replacement projects. Keeping our technology infrastructure up to date is an important component of maintaining efficient operations. While we may need to provide additional funding to make this happen, we will recoup the savings over time and avoid increased costs by putting them off.

One component of our technology infrastructure that we can no longer wait to fund is increasing internet bandwidth and system redundancy to improve reliability. The Proposed FY 2014 Budget includes a plan to purchase internet services from a second service provider. Currently, Cox Communications is the sole internet provider for all city departments and agencies. This plan provides additional bandwidth to support new applications and new facilities coming online, such as the Slover Library and the combined courthouse. Just as important as increasing bandwidth and redundancy, this plan ensures reliable service even during a catastrophic event.

ENVIRONMENTAL SUSTAINABILITY

The priority of Environmental Sustainability focuses on maintaining the community's status as a premier waterfront community that thrives economically and culturally, avoids detrimental environmental impacts while creating a positive, regenerative effect on its environment. One of the main environmental sustainability issues the city faces is flooding. In the Proposed Budget, work continues to address citywide flooding issues.



The comprehensive approach began in FY 2013 to address both precipitation and tidal flooding across the entire city. With the implementation of a long-term tidal and precipitation flooding analysis as well as a shoreline protection analysis, the city is developing solutions for the short-term and long-term. The scope and magnitude of flooding issues, as you are already aware, are beyond the fiscal capabilities of the city alone, and as a result, we are continuing to work collaboratively with the Army Corps of Engineers and our congressional delegation on flooding issues.

WELL-MANAGED GOVERNMENT

The priority of Well-Managed Government is to create a data-driven organization that provides effective and efficient city programs and services that are responsive, accountable, inclusive and customer-focused. Having a well-managed government begins with our employees who accepted this challenge upon my arrival in 2011. Employees are doing their part to make our organization more efficient and effective by working collaboratively across departmental lines to identify more efficient ways of conducting business as well as creating a customer friendly

environment for conducting business throughout the city. These efforts have led to higher efficiency levels, elimination of redundant processes, and reductions in cost of service.

A Conservative Approach to Staffing

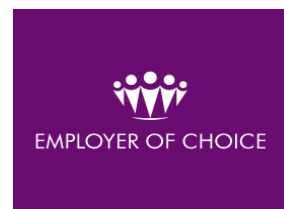
This Proposed Budget has taken a conservative approach to staffing. Other than those related to the opening of the Slover Memorial Library and the reorganization creating the Department of Communications and Technology, the Proposed Budget includes no new permanent positions in the General Fund. Additionally, we have worked to achieve \$1.6 million in targeted personnel reductions. The majority of the \$1.6 million was achieved by eliminating vacant positions and attempting to more accurately project future attrition rates based on historical data. Overall, the Proposed FY 2014 Budget includes 30 fewer permanent positions in the General Fund than FY 2013.

Fleet Management

One area of the organization where we will continue to look to improve operations in FY 2014 is Fleet Management. The restructuring of Fleet continues to promote additional operating efficiencies and employ industry best practices. During FY 2013, Fleet Management's Parts Room was outsourced, creating ongoing savings and allowing for the just-in-time delivery of parts. Additionally, the execution of a body shop contract, the implementation of fixed price fuel contracts and the standardization of staff schedules have all increased efficiencies while keeping costs in line.

Employer of Choice

There are not enough words to express my gratitude to the employees who work so hard to make Norfolk a special place. Each and every day, our men and women put their lives on the line, make personal sacrifices, and bring a commitment to excellence to their jobs.



The Proposed FY 2014 Budget continues support for our employees' work through the Employer of Choice initiative, which was created to attract and retain an engaged and dynamic workforce. The Employer of Choice initiative, announced in the Proposed FY 2013 Budget, included more than just compensation and benefits. A major focus of the Employer of Choice concept is providing opportunities for employees to strengthen their skills for professional growth and development, as well as offer opportunities for cross training and career advancement. The Proposed FY 2014 Budget supports efforts begun in FY 2013 including:

- Tuition reimbursement
- Employer and supervisor training opportunities
- Four hours to volunteer at NPS
- Master Police and Firefighter programs

Additionally, new for FY 2014 is the creation of additional public safety internship opportunities for NPS students and a two percent General Wage Increase (GWI) for all employees beginning

Also, in the upcoming fiscal year, we will undertake a comprehensive review of the city's overall compensation plan for employees. This review will examine best practices as they relate to compensation, additional retirement benefits such as the Deferred Retirement Option Program, retirement contributions, compensation and benefits for permanent full-time employees in the city's lowest pay grades, and conduct a full review of the appropriateness of the Step system.

The priority of Safe, Healthy and Inclusive Communities is to ensure residents of diverse backgrounds and interests feel empowered to come together to assist in the development of safe and healthy neighborhoods that foster a sense of well-being, and make Norfolk a fun place to live, work, and play. Work continues on efforts to improve the quality of life in Norfolk neighborhoods. The Neighbors Building Neighborhoods initiative is being replicated throughout the city and its results to date have attracted the attention of the Hampton Roads Community Foundation. The Foundation, in partnership with the Park Place neighborhood, is proposing to create a 501(c)(3) to continue the work begun under the Greater Park Place Visioning and Engagement Process. As proposed, this initiative will leverage community based resources to meet the specific needs of Norfolk neighborhoods.



A collaborative effort with other Hampton Roads cities and Virginia Supportive Housing is underway to begin the planning for a second single room occupancy apartment complex in Norfolk. When completed, the proposed facility will be the sixth in Hampton Roads modeled after the successful 80 unit Gosnold Apartment Complex located at Gosnold and 25th Street in Park Place.

The city's CIP has served as an important tool for improving not only investment in bricks and mortar, but also supporting activities that promote and sustain our overall quality of life. Before we look ahead to current and future projects, we should understand how past investments have benefited our community. Since 2000, the city has authorized over \$1.0

billion to improve our schools, neighborhoods, public buildings including libraries and recreation centers, as well as repairing and replacing the aged water and wastewater infrastructure.

Moreover, the city's investment has leveraged work in the private sector to improve the quality of life in Norfolk's Neighborhoods that has included the following developments: Berkley Shopping Center that is anchored by a Farm Fresh Grocery Store; the East Beach community; YMCA in Park Place; the public-private redevelopment of Broad Creek; and the Military Highway commercial corridor.

Our CIP functions similar to a credit card. We can buy things today with the promise to repay the lender in the future. While the initial payment to finance the cost of CIP projects may be low, as borrowing increases, the payments continue to grow. Continual borrowing eventually balloons into large annual debt payments years after projects have been approved for funding. Our efforts in prior years to address capital needs through borrowing are now limiting the city's ability to address new capital infrastructure projects.

The city's General Fund CIP is guided by two measures of affordability; one measure is tied to the value of revenue producing real property and the second measure is tied to a proportionate share of the General Fund budget. These measures, or self-imposed debt limits, are as follows:

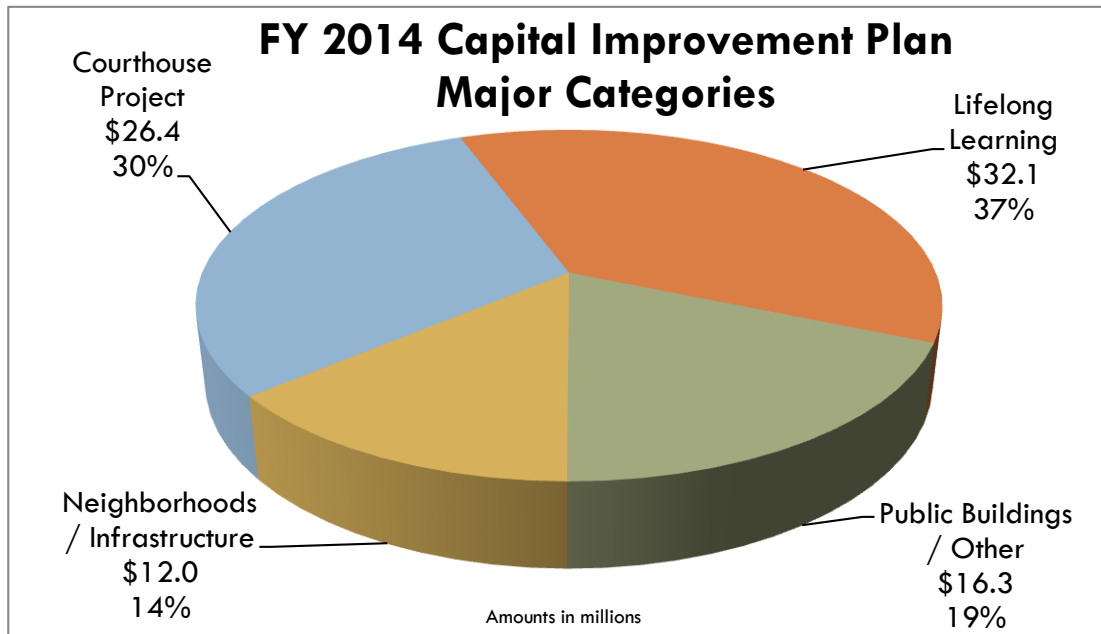
- Debt Service as a percent of the General Fund budget (not-to-exceed 10 percent)
- Net debt as a percent of taxable real estate (not-to-exceed 3.5 percent)

The city will be challenged to stay within these measures as we move forward through the next five years.

The city's General Fund planned projects in the Proposed FY 2014 Budget increase by \$16.1 million from \$70.7 million to \$86.8 million. School capital funding and the courthouse complex comprise 62 percent of the FY 2014 Proposed General Capital CIP. Even with the ongoing funding challenges in our CIP, as a community there is agreement on the urgency to accelerate the construction of school buildings to enhance the learning environment for Norfolk's children. The proposed two-cent real estate tax increase addresses the critical construction, technology, and infrastructure needs of NPS by allowing us to fund the construction of the fourth, Larchmont Elementary, and fifth, Ocean View Elementary, schools in FY 2017. Moving forward with school projects, however, will not relieve the city of other capital obligations related to the citywide infrastructure replacement and repair backlog that we have put off in the past few years.

The city, even with these constraints must continue to address neighborhood needs and infrastructure backlog by allocating appropriate resources to repair, renovate and replace existing facilities. The Proposed CIP restores funding for the neighborhood plans for Broad

Creek, Fairmount Park, Southside and Wards Corner. Additionally, we cannot put off the infrastructure needs of our public facilities any further. As such, funding is provided to address the city's aged infrastructure to extend the useful life of existing buildings.



The backlog of work required on city buildings includes fire stations. The Proposed FY 2014 CIP accelerates the construction schedule for two fire stations that are operating beyond their useful lifecycle. These two stations were originally built as horse-drawn engine companies; Fire Station #12, built in 1924 (89 years old), is located on W. Little Creek Road and Fire Station #11, built in 1925 (88 years old), is located on Verdun Avenue. The Proposed CIP budget moves design of Station #12 into FY 2014, with construction scheduled for FY 2015. Design of Station #11 is scheduled to begin in FY 2015, with construction scheduled for FY 2016.

The rebuilding of these two fire stations will address multiple issues with operating a modern fire-rescue operation in an antiquated building, including difficulties locating equipment, outdated building ventilation systems, and inadequate living quarters that currently do not meet the needs of firefighters. A key to the success of this capital project is the patience displayed by our firefighters in waiting for these projects to get off the ground. I want to thank each and every firefighter for continuing to carry out their duties in a professional manner in spite of the issues they face working in these two facilities.

Similarly, the city's Recreation and Parks system is in need of additional investment to address an aging infrastructure. Under the theme of 'Refresh, Reconnect and Refocus', the Recreation and Parks Master Plan provides a blueprint for improving offerings at city parks, recreation centers, and playgrounds. The Master Plan focuses on the infrastructure backlog through the renovation of existing facilities, with a special emphasis placed on necessary repairs and upgrades. The estimated price tag of the Recreation and Parks Master Plan is \$138 million.

While it will take many years to address the needs identified in the plan, we must address the infrastructure.

CONCLUSIONS AND NEXT STEPS

The Proposed FY 2014 Budget continues the process of building a well-managed government. As we move forward, there are new initiatives we will undertake to improve operating efficiencies in the next fiscal year by completing a comprehensive revision of the city's financial practices and policies.

Also, as part of this review and looking ahead to FY 2015 and beyond, the city's budget allocation decisions will increasingly be impacted by costs that are resistant to change including: debt service, health insurance, retirement, and funding reserves. Identifying appropriate measures to minimize the impacts of these items on future budgets is a priority. Similarly, we will examine personnel packages including a review of various models and best practices that coincide with our efforts to become an Employer of Choice.

Additionally, to achieve long-term fiscal sustainability, throughout FY 2014 the city will continue its review of operations that receive city subsidies: Cemeteries, Fleet Management, and Golf. Review of these operations were discussed in FY 2013 and work has begun to examine options for improving the effectiveness of each operation as well as identifying alternative methods for providing services or determining if the program can be contracted out. These actions are required in order to determine future courses of action, to strengthen financial resources, and to deliver levels of service to meet the needs of Norfolk's residents, businesses and visitors.

Finally, we must keep a close eye on Washington as the impacts of Sequestration loom on the horizon. We will make necessary adjustments as more information becomes available. However, it should be noted, that unlike other cities, we do not have additional resources to put aside funds to cushion potential losses in federal revenue. Our only alternative will be to either cut existing programs or reprogram funding to support the highest priorities.

Even as we discuss issues such as Sequestration, this financial plan, as proposed, provides the necessary elements to keep us on the path to being a well-managed government. We look forward to working with the Council and the community to implement these strategies. Furthermore, it is our belief that these initiatives will lay the groundwork necessary to support the overall quality of life of this great city.

Sincerely,

Marcus D. Jones
City Manager