Fairbanks North Star Borough

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MEMORANDUM

To: Fairbanks North Star Borough Assembly

From: Bryce Ward, Mayor
Bryce Ward (Oct 10, 2023 07:26 AKDT)

Date: October 10, 2023

Subject: Veto – Ordinance 2023-53

Pursuant to FNSBC 2.04.060, I am administratively vetoing Ordinance 2023-53 for the following reasons:

Ordinance 2023-53 creates what is called an "Education Investment Reserve." The reserve as envisioned by this ordinance will effectively function as an endowment, which is not the best use of government funds. The creation of the reserve will increase taxes and will not increase education funding – it will most likely decrease education funding over the short term. This action will replace guaranteed revenue from taxes with speculative earnings and ultimately weaken public trust.

The Government Finance Officers Association (GFOA) defines reserves as "liquid financial resources (typically cash or investments that can be quickly turned into cash) that local governments do not include in the annual spending plan – resources are held back from the budget and held in "reserve" for some other purpose."

The most important purpose for a reserve (according to GFOA) is to respond to significant, unplanned and unavoidable costs. Another common purpose for a reserve is to set aside and accumulate cash to pay for future costs that would not be affordable within a single year's revenue. A capital asset is an example of such a cost.

FNSBC 7.04.075 establishes two codified reserve funds: the Capital Improvement Program and Maintenance Reserve; and the Vehicle and Equipment Replacement Reserve. Each of these reserves has a thoughtfully crafted policy statement on how funds are to accumulate in the reserve and how they are to be utilized for the benefit of providing government services that take multiple years to accumulate adequate funds – for example, fleet vehicle replacements or major facility construction projects.

Ordinance 2023-53 explains how funds are to accumulate within the reserve but fails to provide a methodology for how funds are to be withdrawn from the reserve, other than to state that "All expenditures of these funds must be made by appropriation ordinance" (lines 73-74) and that "these contributions from the Education Investment Reserve to public education should be made using a sustainable draw similar to how the Alaska Permanent Fund draws funds annually" (lines 45-47).

The ordinance language and whereas statements do not explain how the principle of the reserve will be used to respond to significant, unplanned and unavoidable costs or set aside and accumulate cash to pay for future costs that would not be affordable within a single year's revenue stream, such as vehicle and equipment purchases or major facility construction. Instead, the ordinance generally states, "as the Education Investment Reserve starts to spin off reliable and sustainable annual contributions for local education, this will help stabilize and add certainty to local public education funding" (lines 54-56). This leaves the reader of the ordinance to believe that the principle of the fund is not intended to be used for government services but rather, it's the earnings or "spin off" of the fund that will be used to replace "tax revenue as a source of education funding, thus putting downward pressure on the tax burden currently imposed on the local taxpayer" (lines 56-58).

All of this explains to me that the true purpose of the Education Investment Reserve is to build a principle balance and at some time in the distant future, use the earnings of the fund to supposedly add certainty to local public education funding and to replace tax revenue with interest earnings as a source of education funding. The explained intended uses of the Education Investment Reserve in the adopted ordinance are more in alignment with an endowment. An endowment is a donation of money or property to a nonprofit organization <u>which uses the resulting investment income for a specific purpose</u>. Typically, endowments are designed to keep the principal amount intact while using the investment income for charitable efforts.

Accumulated earned interest is used in the budgeting process each year to offset other revenue needed to operate general government services. Historically and on average the Borough has seen interest rates of return on central treasury funds of about 1.5% annually - some years have been higher, and some years have been lower. No matter what the rate of return has been, the Borough has historically used interest returns as revenue to reduce the property tax burden. By allocating this revenue stream from operations to the Education Investment Reserve, we would effectively be increasing taxes by the annual interest return amount or we would need to reduce services by an equal amount. The FY24 budget estimates the Areawide projected interest earnings to be $6.01 million.

The fallacy of this ordinance is that is does not actually increase education funding – it increases taxes for no benefit other than to squirrel away money into an investment fund that is speculative and far less secure than tax revenue with a belief that future returns from the investment account will bring greater returns than if the same money was left to circulate in the economy and be taxed at the time it is needed.

By hoarding large amounts of cash, the Borough runs the risk of losing public trust. According to the sponsors' own admission during a Finance Committee work session, the fund will not have a sustainable amount to draw from for 15 to 20 years, and during that time accumulate a balance upward of $25 million dollars. If the Borough maintains a large reserve and has no documented plans for spending funds in the reserve, local leaders will face criticism from taxpayers. Community members will become frustrated if tax dollars they are paying today do not have a potential intended use in the short run. This can be translated to residents feeling they are being over-taxed.

From a philosophical view, the government should not tax beyond the need to provision services or accumulate large reserves of money, regardless of the source, for the sole purpose of investment. Excess government held funds, specifically tax revenue, would be more efficiently invested and used by local small businesses and residents of the community. I would argue that these dollars give greater returns by staying in the economy instead of being stashed into a fund under the control of the government.

Finally, earnings from an investment fund are speculative while property taxes are almost always guaranteed. If the Assembly sets a revenue budget based on certified values of property, those property taxes are nearly always collected. If a property owner doesn’t pay their taxes, the property becomes delinquent and then goes into the tax foreclosure process where either the property owner becomes current or the Borough eventually sells the property for taxes, penalties and interest owed. Based on tax levy and tax foreclosure processes outlined in Borough code and State law, the Borough’s tax collection rate is nearly 100%.

For these reasons, ordinance 2023-53 should not become law.

cc: Jim Williams, Chief of Staff
Jill Dolan, Borough Attorney

BW/jw