

FRAMEWORK:

**SUMMARY OF FUTURE OPERATING ISSUES
AND RELATED RESOLUTION – FY 2012 THROUGH 2015**

OAKLAND COUNTY, MICHIGAN

November 28, 2011

SUMMARY SCHEDULE - FUTURE OPERATING ISSUES / SHORTFALLS - GENERAL FUND

OAKLAND COUNTY, MICHIGAN
November 28, 2011

<u>Description</u>	<u>Notes</u>	<u>Fiscal Year - (In Thousands)</u>			
		<u>Adopted</u>			<u>Proposed</u>
		<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Appropriated Budget - FY-2012 to FY-2014:					
Revenues	A	\$ 398,730	\$ 378,927	\$ 379,455	\$ 372,193
Expenditures	A	(416,238)	(418,010)	(425,272)	(424,654)
Planned Use of Equity		(17,508)	(39,083)	(45,817)	(52,461)
Beginning Equity at October 1	A	201,162	183,654	144,571	98,754
ENDING EQUITY AT SEPTEMBER 30		183,654	144,571	98,754	46,293
Impacts on Appropriated Budget - Central Tasks:					
Pension contribution projection - net	B	-	(954)	(2,297)	(3,941)
Pension contribution billed to local units	B	-	364	876	1,503
GASB No. 54 - Land Sales Fund	C	(3,541)	-	-	-
Land Sales Fund - Eliminate reliance on planned use of equity	D	998	998	998	-
Fringe benefit rate adjustment	E	4,100	5,466	5,466	5,466
Personal property tax elimination	F	(850)	(850)	(850)	(850)
Diverted felons program	G	-	-	1,700	1,700
Information Technology - equipment replacement	H	-	(1,500)	(3,000)	(3,000)
General favorability / turnover	I	7,500	7,500	7,500	7,500
Longevity impacts - retirements	J	158	412	666	920
Infrastructure needs	K	-	-	(300)	(300)
Motor Pool Fund - return of Gen. Fund working capital	L	500	-	-	-
Indigent medical care - elimination	M	-	-	750	1,000
Net Adjustments from Central Tasks - By Year		8,865	11,436	11,509	9,998
Transfer Net Adjustments in FY-2012 / 2014 to FY-2015		(8,865)	(11,436)	(11,509)	31,810
Net Adjustments Allocated to FY-2015		-	-	-	41,808
PROJECTED EQUITY BEFORE DEPARTMENTAL TASKS		N/A	N/A	N/A	88,101
Targeted Equity at September 30, 2015	N				85,000
EXCESS (SHORTFALL) REQUIRING RESOLUTION					3,101
FY-2012 to FY-2015 budget tasks - None		-	-	-	-
REQUIRED BUDGET TASKS		N/A	N/A	N/A	N/A

NOTE - See footnote and report covering the approach, content and other comments relating to the above Summary Schedule.

FRAMEWORK: SUMMARY OF FUTURE OPERATING SHORTFALLS, ISSUES AND RELATED RESOLUTION OF BUDGETARY SHORTFALLS

OAKLAND COUNTY, MICHIGAN
November 28, 2011

SUMMARY

This initial Framework report indicates that it will not be necessary to assign additional budget tasks beyond those already committed to for the FY-2012 to FY-2015 periods. After the General Fund expends an estimated \$1,671,852,000 over the next four years, the projected excess of revenues (including the use of \$116.2 million in equity) over expenditures is a meager \$3,101,000 (or, a .185% favorable variance).

Clearly, the projected “favorable variance” of just \$3.1 million given the magnitude of the expenditures over the next four years is miniscule, but still positive. Realistically even as the analysis reflects no immediate need to develop new budget tasks, the uncertainty in the County’s future remains high for issues such as the federal healthcare changes, the economy (international, national, state and regional), success of the automobile companies, and the ability of the federal government to address its fiscal ills.

Critical assumptions supporting the conclusion that no additional budget tasks are necessary at this time include:

- First and foremost, prior budget tasks that County’s operating departments have previously committed to must be honored. Any failure to achieve these budget tasks would result in unacceptable shortfalls and would eliminate the projected, razor-thin favorable variance currently anticipated by FY-2015.
- Related to the above, this Framework report assumes that the hiring freeze remains unchanged, the use of part-time, non-eligible personnel are used in lieu of full-time employees continues whenever possible, and that capital projects will continue to receive a high level of scrutiny. New operating programs not funded by grants must be covered by new revenues and / or reductions in existing operating costs.
- That the Gosling Amendment is honored, as it is highly likely that federal grants will experience reduced levels of funding as an ultimate result of the Super-Committee / automatic cuts and the expected continuation of troubled federal operations.

This Framework report describes the favorable and unfavorable operating results for FY-2012 in the General Fund and for those operations impacting the General Fund. When complete and with the fulfillment of the assumptions described, the General Fund equity position should be no less than \$85.0 million, or roughly 20% of expenditures at the end of FY-2015.

BACKGROUND

The schedule entitled “Framework: Summary of Future Operating Issues / Shortfalls – General Fund” (e.g. “Summary Schedule”) and this related explanatory document, are presented based upon financial analyses created by the Fiscal Service and Equalization Divisions of Oakland County’s Department of Management and Budget, various State reports, and other available material. This Framework is a high-level financial planning document that discusses Oakland County’s budgeting process, identifies known budgetary exposures, and sets fiscal and fund equity targets as the starting point in spring 2012 for the preparation of the FY-2015 operating budget.

The Summary Schedule and related analyses rely on the closed September 30, 2011 accounting records, the FY-2012 through FY-2014 County operating budgets as adopted by the Board of Commissioners in September 2011, an analysis of the fiscal matters arising after the adoption of the County’s budget, projections for the future property values used in calculating property tax revenues, and other information. Ultimately, an updated version of the Framework will be produced in early March 2012 after: a.) the Governor’s budget recommendation for FY-2013 is known, b.) the Oakland County property assessment notices are mailed in February, c.) the State’s revenue estimation committee is held in mid-January and d.) the County closes the first quarterly operations for FY-2012.

The Summary Schedule is based on the adopted operating budgets for FY-2012 through FY-2014, inclusive. As planned, the ending equity for the General Fund grew during FY-2011 to allow for the **use** of that equity during the FY-2012 through FY-2015 period. This planned use of equity allows the County to provide stable services to the public, provide security for County employees in their positions and otherwise fulfill the operating goals cited later on in this report. Absent no further actions by County operating departments, the structural operating shortfall for FY-2015 would drive the General Fund equity down to \$57.4 million – an unacceptable level for operating purposes. By FY-2016, the equity would largely be depleted. The very purpose of this Framework is to begin the process of developing actions to avoid the fiscal and operating consequences of the anticipated problems in the next several years.

Proceeds from the planned growth in General Fund equity are being used to cover unresolved structural operating shortfalls through FY-2015. An operating shortfall means the County is spending more than the revenue levels will support. As reflected in the operating budget adopted in September 2011 by the Board of Commissioners shortfalls are \$17.5 million, \$39.0 million, and \$45.8 million, respectively, for the FY-2012 through FY-2014 periods which require a combined total use of equity of \$102.3 million through September 30, 2014 and by FY-2015 a total of \$116.2 million is cumulative planned use of equity. Operating departments are expected to restructure operations over these next several years in order that the presently budgeted shortfalls are eliminated. The operating shortfall for FY-2015 is adjusted in the Summary Schedule for known events, transactions and other information now available as herein discussed.

In these economically turbulent times, the fiscal events and conditions impacting Oakland County's current and future operating budgets are often difficult to project. The assumptions used in this document are critical to its understanding and any actions undertaken through FY-2015. Many assumptions are not controllable by County management and / or the Board of Commissioners, yet some are. Unfortunately, the economic times most governmental units find themselves in are creating havoc in operating budgets with devastating results to core services provided. Absent a methodical long-range financial plan and execution of related departmental actions many other governmental units could find themselves in Public Act 4 of 2011 ("Emergency Manager Act").

As has been the case for years, Oakland County administration continually monitors the budget and actual results of both the current year and future years' budgets. Budgetary adjustments are proposed at every Finance Committee of the Board of Commissioners to reflect changes in operations and / or budgetary assumptions. The County Executive and all County-wide elected officials have managed their operations effectively through the multi-year budgeting process, and have mitigated the impact of adverse an economic environment on County operations, employees and taxpayers – all while services were maintained in accordance with County resident expectations.

BUDGETARY GOALS

The County Executive's budgetary goals, as cited below have continually been achieved by the early adoption of management actions and implemented by operating departments. Cooperation between County-wide elected officials has been and remains critical if the County is to maintain these goals and to minimize the adverse impact of the regional, State and federal fiscal issues on County operations. The cooperation of County-wide elected officials is one of the most important distinguishing qualitative assets contributing to the success of the long-range budgeting process.

Non-312 eligible bargaining groups and Merit System personnel have cooperated as well in accepting budget tasks. This cooperation has resulted in a stable employment base and very few involuntary terminations. Finally, the directors, managers and staff of the County-wide elected officials should be commended in their creative approaches to ensuring minimal operating disruptions and continuous efficiency improvements in services to the public.

Oakland County's methodical, multi-year budget process has mitigated the impacts of the fiscal turmoil caused by events outside its control (i.e., unemployment, property value declines, automobile industry restructuring, the State, federal and local governments' inability to solve their fiscal affairs, etc.). These conditions, however, are significant and if not rectified in the coming years may create a situation that prevents the County from resolving operating budget issues under its control and concurrently meet the goals set forth below in their entirety. To date, Oakland County successfully weathered the fiscal storms and met each of the below goals. If necessary, certain goals may have to be sacrificed to ensure fiscal stability in County

operations. Presently, the County believes it can resolve the operating shortfalls and maintain an appropriate equity level between now and September 30, 2015, with modest operating department actions over this same period.

The County goals include:

- Avoid increasing taxes and fees on County residents and businesses whenever possible.
- Retain stable and essential services to the public while minimizing involuntary employee separations.
- Honor the 'Gosling Amendment' whereby grant programs no longer funded at prior year levels by grantors are reduced and / or eliminated (unless an operating department can specifically identify alternative sources or reductions in costs such that there is no net increase in costs).
- Retain the County's financial strength in stable fund equity and cash positions, provide adequate cash flows throughout the year, and maintain low outstanding debt.
- Restrict the use and reliance on equity and other 'one-time' budget "sources" in solving **structural** operating shortfalls.
- Rely heavily on strong accounting, budgeting and other business practices in achieving long-range planning efforts.
- All new major capital and technology projects are to undergo a rigorous return on investment analysis before they are launched. Projects are to be funded out of current operations to the extent feasible.
- Provide continuous communication with County-wide elected officials concerning the status of the operating budget with emphasis on having the County-wide elected officials solving their share of operating shortfalls without unwanted interference from County administration and Board of Commissioners.
- Address adverse budgetary situations on a timely basis with actions that serve to mitigate the budgetary impact on current and future operations.

To date, these goals have been embodied in operating budgets adopted by the Board of Commissioners and honored by Oakland County and its elected officials. All County-wide elected officials have met their assigned budgetary tasks for restructuring operations such that Oakland County is one of only a few governmental units with balanced multi-year, line-item, rolling (meaning adjusted for known events now and for future operations) operating budgets. Far too many local public officials are recognizing business issues too late, only to result in a

fiscal crisis impacting services to the public, imposing increased taxes / fees, adversely impacting operations and / or incurring involuntary employee separations. Key to the County's success is the cooperation of elected officials and almost all bargaining groups often not present in other governmental units.

PROCESS

The process used in the development of Oakland County's multi-year operating budgets is set forth below:

- **Step 1: Closing of the Accounting Records** – the closing of the September 30, 2011 year end accounting records is the first step in the process for projecting the operating shortfalls, if any, for FY-2015. It is critical to understand the starting point (e.g. equity position as of September 30, 2011) and the projected ending point (e.g. September 30, 2015) in order to develop the operating targets between these two points in time. The accounting records are normally closed in the fourth week after September 30.
- **Step 2: Equity Targets** – equity targets are set for the General Fund and all funds that directly impact the General Fund's operating budget. The initial Framework document is prepared in the first quarter after the multi-year budget passage (in this case, December 2011) in order to provide the County operating departments a sense of actions necessary for FY-2012 and beyond to resolve any FY-2015 operating shortfall. Meetings are conducted with each County-wide elected official or their representative to discuss this initial Framework document in December.

The General Fund ending equity position has generally been set at 20% of the expenditures in the last period under consideration, in this case FY-2015, or \$424,654,000 in FY-2015 expenditures x 20% = \$84,931,000 (rounded to \$85.0 million). Other fund equity targets that impact the General Fund operations are discussed subsequently.

- **Step 3: Assessment of Appropriated Budget and Fund Equity as of September 30, 2011** – the adopted operating budgets for FY-2012 through FY-2014 are currently balanced (including the planned use of equity). The operating and fund equity targets set forth in the Framework document dated March 2, 2011, which were used in the County Executive's recommended budgets for FY-2012, 2013, and 2014, are also believed to be accurate with the exception of the adjustments cited in the Summary Schedule because of the events now known.

Once the accounting records are closed for FY-2011, the projected equity levels in the prior year Framework document are compared to the actual results from the closed accounting records as of September 30, 2011 as a starting point in the process to assess the operating shortfall for FY-2015, along with the setting of equity targets for the coming budgetary efforts as noted in Steps 1 and 2 above.

The **actual** equity levels as of September 30, 2011 in excess of the **future** equity targets as of September 30, 2015, if any, can be used to mitigate annual operating shortfalls for FY-2012 through FY-2015. In doing so, the County has the assurances of having actual equity that serves to reduce the budget tasks assigned to operating departments through FY-2015. For example, if ABC Fund had a target of \$12 million for equity as of September 30, 2015, but had **actual** equity of say \$27 million as of September 30, 2011, then \$15 million (actual > targeted equity three years out) would be available for use in reducing of the operating shortfall in the interim periods – or \$5 million per year ratably for FY-2013, 2014 and 2015.

In this example, by using only \$5 million for the next appropriation period, the second and third years' equity is effectively reserved to address these out-years' budgetary needs and remains in equity as a reservations against adverse events. These reservations would be adjusted in the next year's Framework. This long-range 'rolling' budget process permits an operating department sufficient time to restructure operations in a thoughtful manner rather than being compelled to decimate operations in a crisis mode.

- **Step 4: FY-2015 Projected Operating Budget** – the Framework uses the General Fund's operating budgets for FY-2012 through FY-2014 as adopted by the Board of Commissioners in September 2011 in calculating the high-level operating shortfall for FY-2015. The initial assumption is that **no actions** will be undertaken to correct the operating shortfall to portray the depth of the fiscal issues facing the County in FY-2015 – although clearly the purpose of planning this far ahead is to begin developing departmental action steps to rectify the FY-2015 operating shortfall now.

Included in the calculation of the operating shortfall for FY-2015 are adjustments for central budget tasks that serve to mitigate the depth of the problem before the remaining amount of unresolved operating shortfall is allocated as budget task amounts to County operating departments. The fiscal impacts of these events are characterized by fiscal year.

- **Step 5: Transfer of Impacts** – given that the Framework is solving for the net operating shortfall for FY-2015 of the General Fund, the net increases and decreases in the FY-2012 to FY-2014 operating periods are allocated to the FY-2015 fiscal year in order to assess the net operating shortfall to be addressed today. Early implementation of departmental actions is encouraged.
- **Step 6: Assignment of Budget Tasks to Departments** - the final calculation is the allocation of annual budget tasks required of the County's operating departments from FY-2012 through FY-2015 in order that the equity targets are met as of September 30, 2015 as outlined in this Framework document. The Framework report indicates no new

recommended budget task assignments to County operating departments for the period FY-2012 through FY-2015.

While the above process serves to ensure that the equity targets are obtained as of September 30, 2015, **it does not resolve the structural operating shortfalls for FY-2016 and beyond.** The estimated operating shortfall for FY-2016 is \$46.4 million (before central tasks) and increases thereafter. Budget forecasts for both FY-2015 and FY-2016 were included in the adopted budget document by the Board of Commissioners in September 2011 and will be kept current through the County's 'rolling' process during FY-2012 and beyond at a summary level.

The purpose of the County's budget approach is to provide sufficient time for the County's operating departments to meet the necessary reductions in costs and / or improvements in efficiency that serve to achieve each of the County's budgetary goals. Providing time to address structural budgetary changes in operating departments is critical – given time, the County management can address their interim operating targets to achieve the equity targets as of September 30, 2015.

ECONOMIC ENVIRONMENT

The international, national, state and regional economic uncertainties impacting Oakland County's future operations must be met with disciplined business practices that not only help resolve the immediate fiscal distress, but also resolves them structurally so as to achieve the above operating and fiscal goals. Acknowledging the existence of uncertainties and keeping an ever-vigilant watch for signs of adverse developments is critical to maintaining the County's fiscal strength and in preserving its ability to provide the stable County services the public currently enjoys. The County's strong fiscal policies have provided Oakland County the benefit of anticipating long-range business issues and providing the opportunity to address them before they become a crisis.

Numerous operating and fiscal issues will affect the adopted operating budgets for FY-2012 through FY-2014 and the projected FY-2015 operating shortfall as reflected in the Summary Schedule. Some business issues are out of the control of County officials, but nevertheless must be addressed. In the event of favorable variances against the adopted operating budgets, it is far easier to halt programmatic reductions than it is to impose service reductions deep into a fiscal year. Unfortunately, there are many uncontrollable remaining business risks that could serve to increase the operating shortfall in the next several years.

Because the impact on the Oakland County operating budget is speculative for several of these risks, their impact cannot be included in the Framework or the operating budgets until known with some level of certainty. They are highlighted as cautions to be watched and when sufficient information – either positive or negative – is available, and then appropriate actions can be taken by County management. While no additional concrete remedial actions related to these matters should be currently undertaken, the County is actively monitoring these issues for their impact on current and future budgets. The most significant of these direct exposures

involve the State and federal support of Oakland County programs (e.g. grant program revenues), the State and national economies, and the recently-passed federal healthcare reform. Assumptions will be made involving these risks and documented herein.

Because one or more of these business issues may occur and be unfavorable to the County, it should be acknowledged that future operating shortfalls could be higher than currently estimated. But under this Framework and long-term planning approach, as those business issues become known, they will be addressed by County administration (quite often in the quarterly reports to the Finance Committee). The long-term financial plan would be revised and implemented proactively. If the assumptions and actions taken prove to be overly conservative, revised actions by departments may allow for the restoration of program levels to the extent of the favorable variance or elimination of budget reductions anticipated in future years. Detailed quarterly financial reviews are conducted by the Department of Management and Budget and shared with the Finance Committee of the Board of Commissioners for actions, as appropriate.

International

International issues are having an impact on the national economy and the stock market values (among other causes for market fluctuation). The volatility in the stock market values has significance to the County as declines in the market result in declines in pension and retirees' healthcare investment portfolios. The decline in the investment portfolio from September 30, 2010 to September 30, 2011 for the defined benefit pension contributions are highlighted in Exhibit A to this report starting in FY-2013.

Several international issues, which have recently occurred, impact the County by way of the national economy; such impacts cannot be easily quantified:

- European countries (Greece, Italy, Spain, Ireland and Portugal) are experiencing significant fiscal distress and without restructuring their fiscal affairs may default on their sovereign debt. Defaults on sovereign debt, while rare, have very far reaching impacts affecting even Oakland County. Social and fiscal changes in these countries have been and will continue to be very difficult.
- Presently, Spain has a 22% unemployment rate. Greece has outstanding debt well above its gross national product (an indicator of significant fiscal distress). Italy has just now entered the discussion phase of fiscal problems in the media. The probability of a recession in Europe, one of the USA's primary trading partners, is relatively high in the coming months and years. A recent presentation by an economist from University of Michigan suggests that an infusion of \$1.0 trillion will be required (along with austerity programs) to right the European countries currently in fiscal distress. The source of this \$1.0 trillion was not specified.

- Germany attempted to sell \$8.1 billion in 10-year bonds in late November 2011 but was only able to sell \$5.9 billion at the interest rates offered. Failure of a nation to sell its debt at the then offering rates is an indicator of fiscal issues. In order to ultimately sell its bonds, it will have to raise the interest rates on what was not sold, along with any future bonding needs.
- On November 23, 2011, Fitch (a bond rating agency) lowered Portugal's bond rating to BB+, essentially junk status. Portugal has been actively restructuring its national government operations to more austere operations. Hungary's debt rating was also reduced by Moodys Investor Services to Ba1 (e.g. "BB+").
- While the media has focused on the countries' outstanding debt, the local units of government within these countries are also struggling financially as well. Virtually nothing has been discussed in the media on this matter.
- The Middle East has experienced several wars, changes in regimes and other troubling matters. A primary supplier of oil is from the Middle East. Past disruptions to oil helped trigger the eventual bankruptcy 9 months later of both General Motors Corporation and Chrysler Motor Company. The region and County are still very much tied to the success of the automobile companies, despite movements to diversify.
- China's rise as a global manufacturer also is creating regional and national pressures that will be felt for years to come.

The above issues are completely outside the control of Oakland County but will have impacts in the coming years on the viability of this State and region in which the County resides. The two areas of greatest concern are the volatility of the County's pension and retirees' healthcare investment portfolios and the success of the automobile industry.

Federal Government

Starting with the fall of 2008, the federal government provided two stimulus / bailout packages totaling roughly \$1.6 trillion. There was an additional \$400 billion earmark package in February 2009 and lesser earmarks in 2010 for a combined increase in the national debt of no less than \$2 trillion over a very short time frame. The national debt is over \$15 trillion and increasing at a pace of \$4 billion *daily* (meaning the federal government is spending \$4 billion more each day than it is obtaining in revenues – borrowing the difference).

These federal stimulus and bailout programs tended to benefit banks, state governments and other entities, more than local units of government and in particular, the local governments' general (discretionary) funds. In addition, the State of Michigan used half of its federal stimulus package (\$4.5 billion) to balance its FY-2009 through FY-2011 operating budgets, with no amounts remaining to resolve the FY-2012 operating budget shortfall remaining as the new governor took office (thus, resulting in a budget "cliff").

While the \$4.5 billion in federal support used to keep the State afloat avoided the imposition of State appropriation reductions (e.g. reductions of local government's revenues, including Oakland County) and / or new taxes and fees, it is highly unlikely that the recent shift in Congressional make-up will permit federal support levels seen over the past years to continue – meaning federal reductions in support to the State and local units is probable, but not currently identifiable as to any specific program. There is one area, however, that is apparently already manifesting itself in grant reductions – Community Development Block Grants (reduction of 12% proposed) and the HOME program (loans to County residents; 68% reduction).

While the State has resolved its FY-2012 operating budget with nominal impacts on the County's operating budget, the continued economic condition of the federal government and Michigan is likely to adversely impact County operating budgets for FY-2013 and beyond. Future reductions in support from the State are probable arising from reductions in federal support to the State then passed down to local units. University of Michigan economists have indicated in late November that the high rate of unemployment will remain relatively constant through FY-2013; such condition has implications on what could otherwise have been improvements in property values, State support and direct revenues received from the public by Oakland County.

During the summer of 2011, the burgeoning federal operating shortfall and related borrowing ('national debt') required Congress to adopt increased national debt limits (since August it has moved from \$14.7 trillion to \$15.0 trillion as of this writing). Months of debate led up to the increase in national debt limits. However, as a requirement of the debt limit increase, Congress developed a "Super-Committee" tasked to reduce current and future operating budgets by a cumulative \$1.2 trillion over a 10-year term or, roughly a 3% reduction (\$1.2 trillion / say \$4.0 trillion in annual average spending x 10 years). The Super-Committee has failed to reach agreement on any issue and no present meetings are planned as their statutory deadline has come and gone.

Over the past several months, the Super-Committee has been mired in debates on whether to increase taxes or reduce costs. In late October 2011, the media reported that the Super-Committee could not agree to any of the proposed \$200 billion in budget cuts and one party's proposal on revenue enhancements was unacceptable. The discussions have now shifted to trying to affix blame and finding a solution to, yet again, defer any tough decision on the national operating budget.

The original purpose of the Super-Committee was to secure \$1.2 trillion in revenue increases and / or budget cuts - or, failing that, an 'across-the-board' budget reduction would automatically be applied starting in January 2013 (when the next presidential term begins). While a federal revenue increase would have little or no immediate impact on the County, either a specific program reduction or an 'across-the-board' reduction could have an impact on the County's grant revenues. At this time, however, the County cannot specifically identify either the programs or the amount of potential grant reductions by the federal government

and therefore, has included no provision for any grant losses. Further, the County has the 'Gosling Amendment' contained in all grant acceptances that would require reductions in the affected programs (up to and including complete elimination) should grants be reduced (or, eliminated).

In late November 2011, Moody's Investor Services (a bond rating agency) warned the national government that should Congress rescind the automatic reduction of the \$1.2 trillion program reductions it could downgrade the nation's debt rating. There have already been discussions by the President and members of Congress about the automatic program reductions. Standard & Poors had already downgraded the nation's debt rating going into the summer 2011 debates. With the failure of the Super-Committee, Moody's has stepped up the discussions. A lowering of the bond rating would mean that borrowing costs by the federal government would increase and thereby require additional borrowing to cover the increased interest costs only create another cycle of borrowing / increasing interest costs / more borrowing, etc.

On November 28, 2011, Fitch (another bond rating agency) has assigned the nation's debt a AAA rating with a 'negative outlook' pending the resolution of the across-the-board reductions required by 2013. A 'negative outlook' is a warning signal to the entity being rated that absent actions undertaken to address the underlying concern, the rating agency will downgrade the debt rating.

Alternatively, additional federal borrowing will be required, likely causing an increase in upward pressures on the Consumers Price Index (e.g. inflation). Roughly 56% of all State revenues collected from all sources (including from the federal government and passed down to the local units as 'grant match') are transferred to local units of government to actually operate programs by delivering services directly to the public. This includes Oakland County which receives some \$60 million of its revenue base for programs from these pass-through grants.

While the federal stimulus funds over the past several years did trickle down to the local units, including Oakland County, amounts were restricted as to purpose and not available to solve operating shortfalls in general funds. Typical projects were 'shovel-ready' infrastructure such as for facility construction and road maintenance or cost-reimbursed programs such as workforce development and job training. There is no expectation that future federal program funding will provide unrestricted program dollars to local units of government as they have not done so in the past. Thus, not only the state but many local units of government throughout the country remain fiscally stressed due, in part, to reductions in federal support.

As a result of all of the above, local governmental units must look inwardly to solve their fiscal distress – reliance on the State or federal government to bail out local fiscal distress is now clearly inappropriate. As discussed below, many local units of government in the region are struggling and may see a regional tax-base sharing approach to address the fiscal distress presently experienced in units such as Detroit, Wayne County, Detroit Public Schools, Flint and other numerous other entities.

The Framework's projections assume that national inflation remains in check even as there are actions recently taken by the federal government that could spur inflationary pressures, including the bail out of credit markets, reductions in federal fund rate, stimulus and earmark packages, the 'weak' dollar, the FY-2012 and beyond federal budgets increasing the national deficit by \$1.4 trillion each year, and other similar actions. Some economists have speculated that the real estate market declines are holding down overall inflation even as other components of the Consumers Price Index are increasing, specifically food and gasoline prices. If true and the housing market rebounds, inflation could increase suddenly and rapidly.

The deep recession and property value declines have been keeping inflation in check to date, but at a significant cost to society (and local units of government who are often expected to expand services while governmental revenues contract). The impact of inflation, should it occur, on the County's future operating budgets is unknown. However, if inflation exceeds 5%, then the economic growth rate of taxable value used as a basis for calculating property tax revenues would be capped at 5.0%, even as there would be expenditure pressures to pass inflationary increases onto employees and vendors. Local units of government, including the County, would then be squeezed between increasing expenditures caused by inflation rate increases and its capped principal revenue source (e.g. property taxes which represent roughly 55% of the General Fund revenues).

The federal government passed healthcare reforms that have already impacted the County. For example, 74 new healthcare enrollments for employees' "children" under the age of 26 have been admitted to the County's program. These 'children' were previously excluded by County policy. It is highly likely that the pending Act 312 ruling by the arbiter and state legislative actions could place the County at odds with the requirements under federal law that currently protect the County (i.e. 'grandfather clause'). If the County loses its grandfather status, additional healthcare services not presently contemplated in the operating budgets through FY-2015 are then required to be provided. The dollar impact of the loss of the grandfather status is not known.

In the coming years, there will be other impacts requiring funding. Since full implementation of the federal healthcare law is not expected until 2014 there is an **inability to quantify the impact of the federal healthcare regulations. Thus, no provision for these added costs has been made in this Framework report.** Any changes required that involve needed appropriations in the future would have to be funded out of current revenues and / or budget tasks when known.

Currently, the County has replaced numerous vacant positions with part-time, non-eligible employees (i.e. not eligible for fringe benefits, the most significant cost of which is healthcare). One of the goals of the new federal healthcare legislation is to ensure all employees receive health insurance. In the event that the County must provide healthcare to current part-time, non-eligible employees it will increase the costs of these positions. The rules and regulations for the federal healthcare are still being written, but the limited number of pages written thus far has resulted in a disconcerting number of references to "shall" and "required" (roughly 811

times in the first 244 pages written of regulations, with an estimated 40,000 pages that ultimately will be prepared). No provision for this exposure has been included in the Framework.

In mid-November, the President signed into law an omnibus appropriations bill that cut Community Development Block Grant programs by 12% for FY-2012. The HOME grant program is expected to take a program reduction of up to 68% as well. Both reductions will serve to reduce the grants offered to the local units of government and in a very limited way Oakland County in general. Once the County is formally notified of the specific dollar reductions, the programs will be reduced along with appropriate administrative support if necessary.

According to a Congressional representative in late November 2011, the federal government will be taking up the extension of unemployment benefits in January / February 2012. Roughly 30,000 to 40,000 residents in the State could be impacted; such individuals would lose their benefits should the federal extension not be granted. Undoubtedly, some of the residents live in Oakland County.

Automobile Companies

The automobile companies and related suppliers have been and continue to be under significant cash and operating pressures. At present, the Detroit-Three companies are enjoying increasing vehicle sales, reduced legacy and related fixed operating costs, and a slightly improving market share against the foreign competition. All of these issues bode well for Oakland County over the long term.

The events in the Middle East that resulted in a social revolution and included the ousting long-term leadership and is creating uncertainty in the stock market, especially as oil prices remain volatile. Oil prices are a key component in the inflation calculation. However, what is not readily apparent is the impact on the 'car-buying' public. Will they continue to buy cars in the face of this uncertainty - particularly the higher profit margin cars that often have less efficient mileage rating? If the Middle East unrest adversely affects car purchases, it could manifest itself in production reductions (and thereby adversely impact the County's employment base). The impacts of energy-efficient automobiles also remain unknown.

Several cautions remain in the above improvement:

- **Retirees' healthcare** – while the General Motors Corporation (GMC) and Chrysler Motors Corporation (Chrysler) retirees' healthcare has been restructured in bankruptcy (and likely reduced), the funding of the substantial liability remains unresolved (unfunded actuarial accrued liability as of December 31, 2005 was \$113 billion for the Detroit Three pre-bankruptcy).

The UAW traded some retirees' healthcare obligations for common stock of GMC and Chrysler. The UAW also accepted responsibility to operate the retirees' healthcare

VEBA within the assets and funding arising from post-bankruptcy Detroit-Three operations. The remaining retirees' healthcare obligations are only 30% funded and could become troublesome in the next several years. This funding issue could place fiscal pressures on the healthcare / hospital industry as well. The recently-passed federal healthcare may assist in this issue but this is uncertain.

- **Emission standards** – last year, the federal government announced emission standards for future vehicles estimated to cost many tens of billions in research for 2016 model years (35.5 MPG for the combined fleet; engineering must be completed no later than 2014 to actually produce cars in 2016). Further restrictions by 2025 were also imposed at levels well beyond today's technology and the 2016 standards. In addition, the President has set a target of 1 million electric vehicles by 2015 to be on the road which is increasingly looking as if the target will not be met. California just passed 'cap and trade' legislation based on a version of legislation held up in Congress; the impact of California's action is unknown longer term.

The underlying emissions research and development requires cash that must be expended by the automobile companies *before* the costs are incorporated into the future vehicle prices. Presently, there has been a flurry of activity in securing battery research centers and, ultimately, manufacturers, in an effort to move the industry to the 'next generation' green vehicle, often through governmental tax incentive abatements. Michigan provided 8 companies \$1.2 billion in incentives starting in FY-2013 to be paid over a four year period (a calculation based on the expected number of vehicles to be produced, assuming all are built with Michigan battery companies, would result in a \$4,500 per vehicle subsidy from Michigan residents). All of these entities may not survive as battery technology is coveted by all states and governmental support is being provided throughout the nation.

A recent projection by CARS (Center for Automotive Research, a non-profit entity that provides analysis for the automotive industry) would suggest that when the annual miles per gallon for the automotive company fleets reach between 30 MPG to 40 MPG, the cost per vehicle to achieve that would be in the order of \$5,000 to \$10,000 in incremental investment. Simply put, the return on investment to the car-buying public would not be present. They postulated that there may actually be a "Cuban" type scenario – no one buying the newer fuel efficient cars with 50 MPG and the older cars become more valuable at a lesser MPG. No one can tell the outcome of the significant emissions targets now set by Washington.

- **UAW Contracts** – the UAW contracts, which expired in late summer, have all been passed – thus, avoiding a potential level of uncertainty arising from labor unrest.

Over the past few years, the automobile companies have shed jobs in the State, particularly in this region. The automobile company failures were a prime reason why Oakland County lost 60,000 jobs in 2009. A recent article in the Detroit News cited the expectation that the **region**

should be able to add roughly 30,000 jobs by 2014 – roughly half of the jobs lost in Oakland County in 2009 alone. For the period 2002 to 2013 (estimated), Oakland County has had a net reduction in jobs as estimated by economists from the University of Michigan of approximately 115,700. It takes a job to pay a mortgage.

The loss of a single automotive job, for example, has an economic impact that filters through the economy with additional non-automotive jobs lost (some economists have suggested up to 10 indirect jobs created for each single automotive job). The impact on the State's sales tax, the Michigan Business tax (now corporate income tax in calendar 2012) and personal income taxes is felt almost immediately first **by the State** and then again later by local units as the lost jobs impact property tax values. Because certain local units of government rely heavily on sales taxes (some of which are constitutionally protected) as a basis of their State shared revenues, a decline in the State's revenue levels is also directly felt by these local units.

The impact on local units of government is a bit more troublesome for the above issues. Because job losses do not immediately equate to the loss of a residence or business, the impact on the local unit's principal revenue source – property taxes – can take up to two-plus years to filter through the process that ultimately affects taxable value. Taxable value is the base used in calculating property tax revenues. Once taxable value declines have occurred, they can only be increased by the Consumers Price Index (the lesser of inflation or 5.0%) or 'pop-ups' at the time of a future sale, providing that there is a gap between the assessed value and taxable value at that time. Presently, over 90% of the residential real estate has no gap between assessed and taxable values and therefore, no 'pop-up' would occur. In the west and northern parts of Oakland County, some construction is just now beginning that would provide some net growth in property values subject to taxation.

Assuming a bank seizes a residence / business property for unpaid mortgages, there is an extended period before the residence / business property is placed back on the market and a sale takes place. Once there is a sale, there is no guarantee that a foreclosed property sold by the bank will be included in the next sales study depending on timing. The sales study period for assessment purposes is between October 1 through September 30th ; it impacts the assessment roll for that ensuing December 31st date (90 days after the September 30th sales study period closing date) only to be used in determining the following year's property tax revenues.

This discussion illustrates that the employee job losses (or restoration) will not impact property values for some time to come. It is probable that the calendar 2008 and 2009 restructuring of the automobile companies through lay-offs is a significant contributing cause of the declines in the December 31, 2009, 2010 and 2011 taxable value declines affecting FY-2010, 2011 and 2012 revenues, respectively.

The restoration of jobs, but certainly not at the levels previously seen, will also have a lengthy time frame before it manifests itself in the stabilization of real estate prices through the sales of homes. Sales of business property are likely to lag even further when the economy recovers.

State of Michigan

Michigan will hold its January 2012 revenue estimation conference to provide targeted revenues for the General Fund / General Purpose (GF/GP) and School Aid Funds for FY-2013 and a summary of the estimated results for FY-2012. The Governor will then issue his recommended operating budget for FY-2013 in early February 2012. By statute, the Governor's recommended budget must start with the revenue estimation conference base amounts as agreed to by the House and Senate Fiscal Agencies and the Treasurer in January.

The retirees' healthcare program for State and school district employees has been funded on a pay-as-you-go basis and the annual contribution for these costs have been unfunded annually by roughly \$1.5 billion to \$2.0 billion based on actuarial studies ***each year for the next thirty years***. The current unfunded actuarial accrued liability for retirees' healthcare approximates **\$45 billion**. The underfunded contribution was not funded for FY-2011. The Governor's approved operating budget for FY-2012 provides \$60 million of the GF/GP costs for the first time beyond the amounts on a pay-as-you-go basis; although this is well short of the amount that would actuarially be paid in full.

The aggressive nature of the Michigan Economic Growth Group and Legislature left the State with numerous "tax expenditures" to address. Tax expenditures are defined as revenues that would normally be collected, but have been forgiven against future taxes otherwise paid in the form of targeted and / or refundable tax credits, avoidance of taxes and deductions most often benefitting a small element of the taxpaying public. The tax expenditures have been reduced starting in FY-2012 arising from actions taken by the State in restructuring its tax collections in 2011.

Because the State had never passed a multi-year budget, many of these future events have yet to be publicly discussed in budget negotiations. For example, starting in FY-2013, roughly \$300+ million annually in battery credits have been included in the operating budgets for the next four years, serving to leave a budget hole in the State's General Fund. Tax expenditures have grown from 60% of the amounts billed and collected in revenues to roughly 108% - meaning, more taxes are **not** collected than collected, leaving those who have not received these benefits to fund the operations of State government. It appears that the tax expenditures will largely be eliminated as a means to cover the funding lost by the conversion of the Michigan Business Tax to an income tax on businesses based on the Governor's recommended budget.

Fortunately, as part of the restructuring of the Michigan income and other taxes, the State eliminated many of the tax expenditures and / or capped them. The tax expenditure issue has been mitigated.

Michigan remains fiscally challenged. The Framework assumes that should the State reduce its support of Oakland County-operated programs, a corresponding reduction would occur in the

County-operated program – leaving a net impact of zero on the County’s operations for those programs that are of a cost-reimbursed basis. Essentially, the County under the “Gosling Amendment” will not supplant the State’s support of a program to the extent that the reduced State revenues can be attributed to a specific County program. To the extent that the loss of State revenue applies to grants with no underlying expenditure requirements (Court equity fund, Convention Facilities Development Fund distributions, etc.), these become central tasks that ultimately are assignable to all County operating departments.

Of the revenues collected by the State, 56% of the collections are distributed to local units of government including school districts, intermediate school districts (ISDs), counties, cities, villages, townships and authorities to perform direct services to the public. If the State chooses to address its operating shortfalls by reducing its support to local units of government, these local unit revenue losses will exacerbate an already struggling level of government in providing services to the public. Many local units are struggling to keep a modicum of core services available – not least of which are related to public safety.

By beginning to address the troubled fiscal health of the State, the exposures to State support in the Oakland County operating budget reductions lessen. Said differently, a fiscally healthy State is less likely to reduce appropriations to local units of government, including Oakland County. The proposed budgets for FY-2012 and anticipated for 2013 by the Governor, however, do not have any known significant losses in revenues for Oakland County.

While the State has acted on resolving many of the fiscal budgetary issues with the passage of the FY-2012 budget, the financial condition (e.g. balance sheet) and other issues continue to plague the State and will have to be addressed over the next several years. These issues can affect the County’s operating budgets when being rectified by the State. Indicators that demonstrate the fiscal challenges still facing the State even after the recommended FY-2012 budget proposed by the Governor follow (most of which are cited in the FY-2010 comprehensive annual financial report, CAFR):

- As of September 30, 2010, the State’s General Fund had \$6.2 *million* in cash on hand to cover \$2.3 *billion* in accounts payable (some of which were owed to local units of government). In recent years, operating revenues have been roughly \$7 billion annually.
- As of September 30, 2010, the School Aid Fund had a **negative** cash position (essentially an overdraft had the Fund’s cash not been in a common cash pool). The School Aid Fund borrowed other State funds’ cash of roughly \$1.2 billion. The largest two funds’ cash borrowed by the School Aid Fund was from the General Fund and Transportation-Related Funds (i.e. transit, road repair, etc.).
- Roughly 86% of the General Fund equity at September 30, 2010 is comprised of a receivable from the School Aid Fund of \$887 million. Given the School Aid Fund’s cash position and reliance on the General Fund for operating subsidies, the General Fund’s

ability to obtain repayment is questionable. However, under generally accepted accounting principles, interfund receivables / payables cannot be written off as the State is perpetual even as there is no known way to pay this obligation, nor was it even discussed in the CAFR.

- The State's Unemployment Benefit Trust Fund had a \$3.2 billion deficit (liabilities > assets to pay them, or insolvency) and owed the federal government \$3.8 billion at September 30, 2010. The deficit and debt owed to the federal government has certainly increased over the past year. According to University of Michigan economists, from 2000 to 2009, Michigan had a net loss of 857,000 jobs, almost half of which occurred in the past two years.

The federal government refused to waive the interest due on the outstanding debt (roughly \$106 million for 2011) and required payment during the State's FY-2011. Because the statutory formula used by the federal government for increases in payroll taxes did not cover the required interest payment (let alone any amount towards reducing the principal), the State's General Fund was required to supplement the difference in the amount of approximately \$36 million.

The importance of this matter is that the State will be required to continue to increase its payroll taxes over the next decade until such time as this obligation is paid. Raising payroll taxes when the State is troubled with unemployment creates a hiring barrier, particularly at the lower range of the payroll scale.

- The State's General Fund / General Purpose operating budgets continue to use equity in order to balance through September 30, 2013 as reflected in the two Legislative Fiscal Agencies' reports dated February 2011. As reflected in the Governor's recommended budget, by the end of FY-2013, the equity position is expected to be \$12 million – just 12 hours of equity.
- As an indication of the deficit problem for the State's Information Technology Fund, had the deficit of \$154 million as of September 30, 2010 (e.g. liabilities > assets) been entirely funded by the State's General Fund in FY-2010 at that time, the General Fund unreserved equity would have been reduced down to \$52 million for an \$7 billion operation – or, roughly 65 hours of equity. The Information Technology Fund deficit arose because of the continued reductions of General Fund expenditures (e.g. the Information Technology Fund revenues), but no reductions in computer services. How the deficit in the Information Technology Fund was to be resolved was not discussed in the CAFR or recommended FY-2012 operating budget.
- Pension contributions have been shorted for the State and school district pension plans by \$1.4 billion over a period from fiscal 2002 to 2010 contributing to the unfunded amounts in the pension plans. In addition, the investment portfolio losses in FY-2008 and FY-2009 could start to adversely impact the pension contributions circa 2012 and

beyond. The FY-2012 pension contributions required of school districts was increased by quite a bit; such increase covered in part the failure to fully fund annual pension contributions through much of the past decade. Likely, the pension contributions will be elevated for quite some time in order to solve this lack of pension contribution funding over the past decade.

- The unfunded actuarial accrued liability for the State and school retirees' healthcare plans is roughly \$45 billion as of September 30, 2009. The State has funded this obligation on a 'pay-as-you-go' basis through FY-2011 but set aside \$60 million starting in FY-2012. Had the State funded these plans actuarially, the added retirees' healthcare contribution (e.g. over the \$200 million now being set aside) would require \$1.5 billion to \$2.0 billion in addition to the FY-2012 operations and beyond – ***in each year for the next thirty years.***
- The reductions in State support to local units of government (and schools in particular) in FY-2010 through FY-2012 were substantial, along with a significant increase in amounts billed to the school districts for pension and retirees' healthcare costs. Statutory revenue sharing payments to local units of government were reduced by one-third for FY-2012. Along with property tax revenue declines, the reduced State support will contribute to local units falling into deficit positions (e.g. liabilities over assets) contributing to substantial cash flow shortages (likely in the spring periods once imposed). Several local units have currently considered filing for federal bankruptcy.

The timing of the future cash flow shortages – spring2012 – is critical for counties (those out of revenue sharing trust fund proceeds), cities, school districts, intermediate school districts, charter academies, and the State. Many local units will be seeking cash from risk-adverse banks even as their credit ratings are troubled.

Numerous local units of government are now struggling in the region. Pontiac is now in Public Act 4 of 2011 (emergency manager act), Royal Oak Township failed to secure a 5.0 mil increase in property taxes, several school districts in Oakland County are on the Michigan Department of Education 'watch list' as their general funds have an accumulated deficit and many other local units have succumbed to laying off public safety officers (one of the last areas normally reduced by local public officials). It will be difficult for Oakland County (the 'entity') to remain strong if subordinate local units of government are weakened by the State and federal government's reduction of operating support and by property tax revenue declines. Even if the local units should arguably be restructuring their services to respond to the lost State support and property tax revenues, it takes time to do so and far too many have waited too long to start.

After the passage of Public Act 4 of 2011 (a law that strengthened the former Act 72 – emergency financial manager act), several community groups sponsored a ballot initiative that has garnered support for Act 4's repeal. At the present rate of obtaining signatures in favor of repeal, it is conceivable that by late calendar 2011 there may be sufficient signatures to hold Act 4 in abeyance pending the August 2012 ballot. It is presently believed, but would certainly

be challenged in court, that the Act 72 would be reinstated. Absent Act 4 (or even the weaker version, Act 72), all barriers that contributed to the local units fiscal distress would be reinstated along with the elected officials at a time when the cash flow for many local units is at its weakest point in the fiscal year. Some local units of government may not have sufficient cash to operate in the coming months.

Finally, the State has recently passed Public Act 152 of 2011 that provides for limitations on the funding of healthcare costs by local units of government, with the excess paid by the employees. The Board of Commissioners recently passed a waiver in accordance with provisions of Act 152 for the 2012 calendar year and as such, there is no calendar year 2012 impact relating to this legislation.

The County administration is moving actively to restructure its healthcare offerings to employees in order to provide a decent healthcare package attractive to both employees and potential employees, yet live within the new State requirements. By spring 2012, the County is hopeful in completing this analysis and will be able to identify the impacts on calendar 2013 and beyond operations. At this time, this legislation would either result in no budgetary benefits or some benefits to the County; therefore, there should be no immediate concerns as to unquantifiable budget risks on the Summary Schedule. By the time the updated Framework is completed in winter 2012, a better status will be able to be provided along with any budgetary impacts.

In summary, the Governor's recommended budget submitted on February 17, 2011 for FY-2012 and as adopted in spring 2011 has indicated that there are no significant adverse financial implications on Oakland County's operating budget. Unfortunately, local units of government, the ISD and school districts have lost significant State support upon adoption of that budget – thus, weakening the local units of government fiscal health.

Other State issues to watch in the near term follow:

- The State should close its accounting records in the next several months and publish a comprehensive annual financial report by March 2012 for the fiscal year ended September 30, 2011. This audited financial report, the revenue estimation committee in January 2012, and the Governor's recommended budget would be helpful in finalizing the FY-2013 operating budget and beyond. The current information coming out from the State is piecemeal and difficult to assess until the full picture is presented in 60 to 90 days.
- In July 2012, the State will publish a study involving the public defense of indigent offenders which is currently funded by local units of government. Lawsuits have been filed and substantial pressures have been building over the past several years to improve this service. The added costs and how these costs would be funded are unknown. No provision in the Summary Schedule has been made for this matter.

- The personal property tax revenue is currently under discussion for potential elimination by the State, either in whole or part. Personal property tax revenue provides \$15 million in annual revenue to the County's General Fund. Of the three components (commercial, utility and industrial personal property), the industrial values are presently receiving the most attention for elimination; such loss has been incorporated into the Summary Schedule and discussed subsequently. Basically, the industrial values of property in existence for December 31, 2011 have been phased out as the property is depreciated and no new additions to value has been provided effective January 1, 2012.
- House Bill 5112 covering the Court equity fund distribution includes a fair amount of changes to the processing of this revenue at the State level. The Court equity fund annually provides almost \$6.0 million in discretionary revenue to the County's General Fund. If passed by the Legislature, the County's Circuit, Probate, and 52nd District Courts would have to develop plans to improve its technology, collaborate with other courts, and provide a dashboard or other means of transparency in order to secure these funds. These funds are no longer as assured as they have been historically. No provision for the potential loss of this State support and / or increased costs resulting from new operating requirements has been included in the Summary Schedule through September 30, 2015.
- Pressures on grant programs arising from the fringe benefit rate increases (see subsequent discussions) and desire by the federal and State governments in the reduction of their operations, it is likely that the indirect cost allocation revenue obtained by the General Fund for services provided to all County departments will be under challenge – either directly via limitations that can be billed to the grantor or through a 'crowding out' of grant program operations. The Summary Schedule has provided no provision for indirect cost reimbursement losses, even as this area provides some moderate risk of loss in the coming years. This area warrants constant review to assess the federal and State grantors' desire to continue to fund these costs.
- Despite repeated efforts to secure support for legislation that would inhibit the pass-down of unfunded mandates on local units of government, the State has successfully resisted the unified position of counties, cities, villages, townships, schools, intermediate school districts, community colleges and road commissions to pass such legislation. While bills have been introduced in the House in calendar 2012, there has yet to be a single hearing and none is presently scheduled.

The Southeastern Michigan Region and Oakland County

Oakland County administration launched numerous economic development and job retention / location services that have assisted in mitigating some declines in County and local unit revenues. Programs such as Emerging Sectors, Automation Alley, Main Street, Medical Main Street, and Oak Street have and will continue to improve the quality of life for all residents,

businesses and those who visit Oakland County. The severity of the economic decline, however, highlights the importance of these programs.

Over the last decade or so, the County launched many technology initiatives that have served to improve the efficiencies of County and local unit operations. For example, the COPS MORE grant received in the late 1990s resulted in a revamping of all aspects of the CLEMIS program (a local computer program involving roughly two dozen applications targeting the prevention of crime). The CLEMIS program resulted in saving the region (Wayne, Macomb, Livingston, Washtenaw and Oakland Counties) over 2,400 law enforcement officers through its efficiencies – said differently, had the program not been undertaken, the depth of layoffs of police officers in this region would have been nothing short of catastrophic. Numerous other technology programs, County supported in whole or part, have benefitted local units of government in this region.

The depth of the fiscal issues arising from the declines in taxable values and the State's resolution of its fiscal affairs has become more readily evident to local public officials and County residents as services were reduced or voter requests for millage rate increased on recent ballots. Many schools are troubled and have few options available to them; 43 school districts were on a watch list in the fall of 2010. School districts cannot raise a local operating millage due to Constitutional limitations and the FY-2012 operating budget reduced State support and increased pension / retirees' healthcare costs. Other local governmental officials will be reviewing their options given declines in property values. It is safe to say that the resolution of these two issues – taxable value declines and reduced State support of local units (coupled by federal deficits / borrowing) – has exacerbated many local units' ability to provide stable, core services to the public.

Competition for scarce governmental resources is fierce and increasing. In addition to the above fiscal pressures created by taxable value declines and State revenue reductions, other service needs and pressures face local and State public officials – all of which will require additional resources and / or reallocation of existing resources easily into the billions of new dollars. Even as many local units cannot field a full complement of police, fire and emergency medical services personnel, constituency groups and public officials are still advocating for expansion of ***new programs with new funding***, as noted below:

- **Transit.** Regional transit for light rail for new services could cost up to \$10 billion for the capital costs alone (only a portion of which would be funded by the federal government). The local share of the capital costs and subsequent operating revenues have not been identified.

In a meeting held on November 14, 2011, the SMART Board reduced its services in response to declining property values (and thus, related revenues) and State and federal support. Effective mid-December 2011, 123 positions (mostly filled) will be eliminated and routes curtailed or completely eliminated as well. In addition, a recently-passed Public Act 54 of 2011 has placed SMART out of compliance with the federal regulations

(thus, exposing SMART to a loss of \$19.5 million in operating grants for FY-2012 and \$12 million in capital grants placed on hold – and in the interim, the cash flow relating to each). SMART needs to begin acquiring over \$100 million in new buses but has little or no funds, absent federal capital grants, to do so; such grants are roughly \$5 million annually.

The Detroit Department of Transportation (DDOT) is experiencing similar fiscal issues as it attempts to live within a shrinking City of Detroit revenue base. DDOT services have been reduced (which adversely impacts SMART and has caused SMART to lose \$900,000 for the FY-2009 service declines of DDOT). The lack of maintenance at DDOT has caused a reduction of the number of buses in operation. At this writing it remains unresolved.

SMART may be seeking a millage increase in the August 2012 election for the July 1, 2013 levy (FY-2014 revenues). The amount of the increase is unknown. In the past election, Oakland County extended its millage at .59 mils for two years while Macomb and Wayne County's elections were for four years. Oakland County's millage on the August 2012 ballot will include not only the .59 mils but whatever is finally determined as necessary under the circumstances. Macomb and Wayne Counties will have to *supplement* their four-year budget of .59 mils to provide parity with the Oakland County budget.

The State is seeking a regional transit solution and is considering a voter-approved increase of up to \$40 per car registered in the region for expanded service, even as the core services of both SMART and DDOT are faltering. The federal government is pressing hard for a light-rail line on Woodward, even as they have provided assurances that there is an insufficiency of federal grant dollars to do so. The issue remains unresolved but, if solved in the near term, it is clear that the August 2012 ballot may include two proposals – extension and increase of the SMART millage for existing services and a regional transit ballot initiative.

While voter tax fatigue is still possible, the last two elections (the most recent one in November 2011) involved numerous property tax questions, largely in support of public safety and libraries. Most of the tax questions were approved. Whether tax fatigue sets in and when remains an open question.

- **Infrastructure.** As cited in a recent memorandum from the Governor, the maintenance budget for roads, bridges, highways and other infrastructure are in dire need of added funding. The Governor offered a potential solution of an added vehicle registration fee of up to \$120 per vehicle annually, restructuring of the underlying gas tax and organizational changes at the County level (for example, moving the County's Road Commission formally under the County Executive / Board of Commissioners rather than as a separate entity). This proposed fee, which very well could also be included on a ballot in August 2012, is in addition to the transit fees noted directly above.

- **Environmental Clean-up.** In a news article dated December 12, 2010, approximately 11,000 contaminated sites were noted as requiring environmental cleanup. While \$1 billion was raised in two previous bond issues (1988 and 1998), the bond proceeds resolved roughly 1,000 of the sites and are largely expended. Environmental groups will be pressing for an increase in the sales tax on the 2012 ballot.
- **Water / Drain Projects.** The compliance with federal mandates continues to create needs in the hundreds of millions of dollars, if not billions. The Detroit Water and Sewerage Department lawsuit of 34 years has recently been transferred to a new federal judge with the passing of the former judge. The new judge recently ruled on a new regional governance structure that may garner some formal objections from City officials and residents. The matter remains open.
- **Fiscal Distress.** The fiscally faltering local units of government with declining operating support from the federal and State governments and reduced property taxes have created pressures to find resources to solve this problem. Several millage increases are finding their way onto ballots with each election; school districts, however, cannot float operating millages under the Constitution.

Cities, villages, counties, school districts and Oakland Schools have similar cash flow pressures during the same time of the year January through June 2012. With the loss of property taxes, several local units are routinely asking for millage increases, the absence of which may mean substantial program reductions and increasing fiscal distress for the local units. Even as local units seek increased millage rates, the successful ballot initiative could 'crowd out' other new funding for the programs cited herein – essentially, at some point, voter rejections of millage and other fee increases will occur.

Wayne County, the City of Detroit and Detroit Public Schools (DPS) continue to add to their accumulated deficits based on either the recently-released comprehensive annual financial reports or media reports to the tune of hundreds of millions. This situation cannot continue indefinitely and must be resolved either through Act 4 (the DPS is already in Act 4 and Detroit's Mayor has initiated discussions on this matter) or through other substantial restructuring of operations, potentially in regional initiatives. The fiscal distress of these three entities could impact the County over the next several years in a manner currently unknown.

- **New Bridge.** Over the past several years, the State debate for a new bridge to Canada was fierce. Estimates of up to \$2 to \$5 billion have been cited for its construction. Even as the bridge is expected to be funded from crossing fees, State guarantees might be required in order for the debt to be issued – meaning that should the fees be insufficient, the State may be required to make up the difference, even with assurances to the contrary. While a recent attempt at establishing an authority did not pass in the Legislature, the matter is far from over. The resolution of this matter on the region is unknown.

- **Cobo Hall.** Even as the State launched the Cobo Hall project with the State’s financial projections (Oakland County objected to the proposal as inadequate to sustain Cobo Hall operations in the long-term), the new Cobo Hall authority has discovered that the anticipated revenues may be insufficient to cover the future debt service and operations starting in roughly two to four years. The Cobo authority has sought Oakland County’s support in restructuring the Cobo Hall legislation to cover the future debt service and operating costs – in order to issue the full amount of bonds for the improved facility. No support has been provided pending legislation that has yet to be drafted with assurances that the County’s Convention Facility Act revenue (roughly \$3.4 million annually to the General Fund) remains intact.
- **Red Wings.** The Red Wings have periodically considered a move from the current facilities to a new facility. Discussions are only preliminary.
- **Social Needs.** Social needs and related issues (child care, domestic abuse, housing, food, and other general welfare needs) continue to increase even as resources continue to be stressed to provide appropriate support. The State recently capped the general welfare support benefits at 48 months and the length of time benefits could be paid on unemployment; the impact on the region has yet to be felt. Likely, non-profits are struggling in meeting the demand.
- **Detroit / Wayne County.** In late November 2010, Wayne County lost a lawsuit brought by the Wayne County Circuit Court in the funding levels required to properly maintain a circuit court operation. The St. Clair Circuit Court awarded the Wayne County Circuit Court an amount, as estimated by the Wayne County Executive, of potentially up to \$500 million in added personnel and facilities – even as Wayne County has an estimated deficit in its General Fund of \$266 million as of September 30, 2010 and growing. This lawsuit has been appealed by the Wayne County Executive. While it is expected to be overturned, to some degree, the effect on funding levels for all circuit courts in the State is currently unknown.

The Mayor of the City of Detroit has recently announced that the City is severely fiscally distressed. Proposed program reductions and / or revenue increases may not be sufficient to stave off the imposition of an emergency manager. Even if the City’s public officials can avoid an Act 4 imposition by the State, the longer term image issues on branding this region a habitable place to locate both companies and employees has been tarnished. A further erosion of the fiscal health of Detroit will impact the County’s south-end directly, but an overall impact will be felt as the State tries to address this issue in ways yet to be determined.

Clearly the convergence of the tax increases for new programs and increasing needs for the “core” programs are going to create angst in Oakland County’s taxpaying community. The national government, state and local units are debating the need for new taxes and / or

significant reductions in programs offered to the public. Within a relatively short order, even with valid programs, in a national and State economy exhibiting a weak recovery, the taxpaying public may well say, “no more taxes” at the ballot box – the Tea Party was borne out of this very taxpaying frustration and resulted in a significant party shift in Congress and State in November 2010.

Even as the County provided funding for professionally-prepared feasibility studies for consolidation / service sharing agreements between two or more communities, little return on the investment was realized. Most local units failed to implement what could have saved millions in avoided operating costs, even as they continue to experience fiscal pressures to provide services against declining resources. The County’s program had been funded through the Capital and Cooperative Initiatives Revolving Fund (CCIRF) but, given the refusal of local units to embrace proposed changes, no appropriation was provided effective October 1, 2009 forward and the CCIRF is being eliminated. Despite the fact that the ability of local units to secure full statutory revenue sharing depends on plans to demonstrate collaboration with their neighbors several proposed consolidation proposals were rejected. The County administration, therefor, has no intention on requesting any new funding for this program.

Even as the local units have not addressed many of the impending problems in property value declines and upcoming further reductions in State and federal distributions, the property tax claims in front of the Michigan Tax Tribunal (or MTT with 46,000 cases statewide) **will** result in even further downward fiscal pressures in 2011 and beyond. Presently, the amount of property value under challenge in Oakland County has declined (in part, because of the interim resolutions to the MTT cases during the year). Unlike far too many local units, the County adequately provided for the anticipated losses in the County’s General Fund reserves.

MTT value losses have a twofold problem: in the commercial sector (and the largest potential losses), the amounts almost always require refunds of prior collected and often spent property tax revenues, to be paid for out of a reduced taxable value going forward. One such recent example was in the City of Flint where two automobile plants were revalued from \$100 million in taxable value to \$27 million, with a *negotiated* refund of \$1.3 million (roughly a third of the ‘real’ amount then due) with maybe \$3 million less in revenues forthcoming in future years on these two plants. The potential for local units not having anticipated and provided reserves on these future losses is extremely high.

Local units are at risk for the MTT property value losses relating to commercial, industrial and retail properties located in Downtown Development Authorities, Tax Increment Financing Authorities and similar entities that have issued long-term debt in anticipation of *increasing* taxable values. Many of these authorities have only enough to pay debt service with no reserves retained. Given the MTT losses will be experienced in FY-2011 and beyond even as the available property tax revenue in these entities decline, these local units may be unable to cover the future debt service costs with the revenues generated within these authorities – further exacerbating the local units’ general funds, programs and / or even potentially resulting in these units defaulting on debt service.

ASSUMPTIONS

To the extent feasible, Oakland County's FY-2012 through FY-2014 budget (as adopted by the Board of Commissioners in September 2011) planned for all business issues that would be impacted by actions at the national, State and regional levels and provided for adequate operating and equity targets into FY-2015. The operating budgets for FY-2012 through FY-2014 were adopted by the Board of Commissioners in September 2011. While the County has been successful in meeting its equity targets, the projected operating budget for FY-2015 must be considered as part of this Framework.

The above business concerns exist for the national government, State and regional local units of government and require current action through adjustments to the Oakland County's operating budgets as adopted by the Board of Commissioners in September 2010 for FY-2011, 2012 and 2013. The principal assumptions, some of which are being adjusted arising from this Framework document, must be retained during the FY-2012 through FY-2015 period in order to achieve the equity targets.

The principal assumptions follow:

- **Property Taxes.** Property tax revenues incorporated in the September 2011 adopted budget are based on an unchanged millage rate of 4.19 mils and a taxable value decline of 3.0%, 1% and 0.0% for the assessment roll on December 31, 2011, 2012 and 2013, respectively and representing property tax revenues for FY-2012, 2013 and 2014, respectively. The FY-2015 property tax revenue increase for the operating budget adopted by the Board in September 2011 was 2.0%.

Even while the property tax revenues continue to decline, the property tax revenues have improved on a county-wide basis simply because they are not declining at the same pace as the rates seen over the past several years. The less than expected declines in the anticipated property tax revenues serve to reduce the FY-2015 operating shortfall.

At present, there is likely more of an upside to the improvements in taxable value than further declines. Mortgage foreclosures are declining – projected at roughly 7,500 for calendar 2011, down from 9,300 in 2010. To place this in context, the tax foreclosures during the 1990s were roughly 800 *annually*. Some construction is starting in the west and northern sections of the County. Established communities (Birmingham, Bloomfield Hills, etc.) are holding the taxable values around zero or increasing slightly. Older communities such as Pontiac and those in the south end, however, continue to experience taxable value losses, some at very high levels (Pontiac, for example, is expected to lose roughly 14% in taxable value from December 31, 2010 to 2011 reducing FY-2013 revenues).

Overall, property taxes should be viewed cautiously as there are still significant national exposures for a double-dip loss (e.g. another bubble bursting). A 2011 BusinessWeek article indicated that of the 800,000 mortgage foreclosures in the nation, over 230,000 are held by Fannie Mae, Freddie Mac and the Federal Housing Administration. These three entities are divesting themselves of the mortgage foreclosures at whatever price can be obtained. The overall question remains – if the banks and federal agencies dispose of mortgage foreclosures in an orderly fashion, the value losses discussed above should be able to be restrained. If there is a desire to quickly dispose of the property, then losses above that estimated in the budget will occur. The County's budget assumed a responsible, orderly process of disposal for the foreclosed properties held by banks and the federal agencies.

At present, a 1.0% positive change in the assumption base for December 31, 2012 over the 2011 assessment roll would result in additional revenues for FY-2013 and each year thereafter of \$1,962,646.

- **Salary Increases.** The October 1, 2010 salary reduction of 1.5% (FY-2011) was applied to all County employees except those in Act 312 bargaining units. The Act 312 bargaining units refused the reductions and are in binding arbitration. A decision should be issued in late 2011 or early calendar 2012 and should be available for inclusion in the final Framework document. A 1.0% increase in salary equates to roughly \$2.0 million in added costs. If applied to all, it allows for the retention of roughly 30 positions that otherwise may need to be eliminated involuntarily. Effective October 1, 2011 and 2012 (for FY-2012 and FY-2013 operations), there are no proposed raises in the operating budget. For October 1, 2013 (for FY-2014) an increase of 1.0% has been projected; with 1% increase on October 1, 2014 for FY-2015.

An Act 312 arbiter's decision was recently received for Oakland County's Command Officers bargaining unit has recently settled, but with 'me too' salary arrangements with the Deputies bargaining group. As noted, the Deputies bargaining group remains in Act 312 (arbitration) and the decision of the arbiter is likely several months off. The Deputies bargaining group is, to a large degree, comprised of employees who patrol local units of government under patrol contracts. Any increases in costs arising from this bargaining group's Act 312 award would largely be burdened on the contracting local units of government as a 'pass-through' and will not be charged as a net cost to the General Fund. About one-quarter of the Act 312 eligible employees are direct General Fund employees.

Given the uncertainty surrounding this matter, no provision has been incorporated in the Summary Schedule at this time. The arbiter's decision will undoubtedly be rendered by the time the final Framework document is issued and will be incorporated therein.

- **Healthcare.** The assumption included in the period FY-2012 through FY-2015 is that the level of healthcare costs for active employees and retirees will remain controlled over

the next several years. The Administration has incorporated a reasonable level of increases to the cost base for FY-2011 through FY-2014 for inflation, including healthcare inflation at 6.0% for each year, a level above that set for other inflationary increases for vendors and similar operating costs.

As noted, there has been an analysis of the fringe benefit rates used to cover the County's necessary and actual costs in the Fringe Benefit Fund. During the past several months, several grants have experienced operating issues because the fringe benefit rate currently charged exceeds that which the grantor allows of that can be charged without reducing the overall programs. Adjustments in the Summary Schedule have been proposed in the fringe benefit rates presented herein

Perhaps the most significant exposure to the County involves the federal healthcare legislation where rules and regulations are still being developed. Without the underlying rules and regulations being written and known, it is virtually impossible to assess the impact on the FY-2014 operations and beyond (the date when most of the impacts will first be felt on the County's operations).

Given this limitation, the assumption for the Summary Schedule reflect no incremental costs for FY-2014 and beyond, even though under the circumstances the programmatic impact include abandoning County-offered healthcare (at a penalty of roughly \$3,000 per person under a federal program) to added costs caused by additional individuals affecting the costs in the market place and expanded coverage required under federal law. No one can adequately predict the impacts on future healthcare costs so that a meaningful projection can be made; however, the potential cost impact on the County remains one of the more significant unquantifiable budget exposures.

The changes for the State's implementation of Public Act 152, which imposes limitations on funding of healthcare plans paid by the employer / employee, has been reflected in the Summary Schedule and explained subsequently.

- **Hiring Freeze.** The County has had a strict hiring freeze with emphasis on operating departments either eliminating the position or if at all possible, replacing it with one or more part-time employees. In addition, to minimize job loss and unemployment costs, efforts have been undertaken to fill full-time vacant positions, to the extent feasible, with existing employees whose positions are being deleted.

This effort of retaining positions to the extent feasible undoubtedly went a long way in securing salary rate reductions over the past several years. However, the general movement from full-time equivalents to part-time non-eligible equivalents, the reduction in salaries arising from roughly 300 employees not being replaced and reductions in salaries of 4.0% over the past several years, while significantly saving taxpayer dollars, have resulted in under-absorption of the fixed costs incurred by the County's Fringe Benefits Fund. These costs are largely the debt service payments on the

Certificates of Participation debt to fund for the retirees healthcare costs). Rate and other adjustments have been necessary over the past several years in the expenditures of operating funds and thus, revenues for the Fringe Benefit Fund, to ensure that the debt service is covered.

The intensive review of every position's replacement is a significant reason why the County has recently experienced sizable favorable variances in many departments. In the spring 2011 Framework, the County planned for \$5.0 million in annual favorable variances; yet the actual variances were much higher than the prior Framework assumed. As noted, the favorable variance amounts (largely turnover) have been increased.

- **Launch of New Programs.** There are no new operating programs directly funded by General Fund revenues being proposed or implemented other than those that will provide a monetary return on investment in productivity improvements (e.g. "return on investment") over the next several years and / or are covered by grants.
- **Gosling Amendment.** All lapsing grant programs of a cost-reimbursement nature adhere to the "Gosling Amendment" that (requires the program costs to be eliminated, including personnel, if financial support by the grantor is withdrawn).
- **Capital Programs.** No new capital programs that require funding from the General Fund are launched absent those that provide a monetary return on investment in productivity improvements or are required by mandates. Capital program activities are limited to repairs and maintenance of existing facilities and infrastructure (parking lots, roofs, boilers, HVAC, etc.) for the next several years and are within the available resources in the respective facilities' funds.
- **Budget Tasks – Operating Departments.** Any remaining budget tasks for County operating departments in FY-2012 through FY-2014 must be honored – either by the original commitment or an equivalent dollar reduction in a revised, future budget task.
- **Property Tax Calendar.** The revisions to the property tax calendar as imposed on counties by the State in 2005 will eventually require all counties to borrow for a new cash flow hole of roughly 7 to 10 months of expenditures that will be incurred (October 1 through June 30th) before the property taxes levied on July 1 will start being received (roughly 45 days after the levy date of July 1st). The cash flow borrowing arising from the changes in the property tax calendar of 2005 will not start impacting the County until 2013 and phase in through 2015 in increasing amounts as the revenue sharing trust fund (e.g. cash) is depleted. In 2013, the County may have to start borrowing short-term for operating purposes for the first time in its history (other than for the Delinquent Tax Revolving Fund short-term notes used to finance the delinquent receivables).

A provision for interest costs has been incorporated starting in FY-2013 and increasing thereafter in anticipation of the State eliminating revenue sharing in FY-2015. Given the State's changes in the statutory component of revenue sharing for counties through the reduction of roughly one-third of the base, Oakland County is expected to lose \$8.2 million in its State revenue sharing support starting in FY-2015 when the Revenue Sharing Trust Fund (RSTF) is completely depleted. The County expects that the State will provide revenue sharing at a lower level, roughly \$16.4 million, annually thereafter, after the use of roughly \$11 million in remaining RSTF proceeds in early FY-2015.

- **General Fund Equity – Uses.** Other than the amounts designated for budget transition (e.g. covering of operating shortfalls in FY-2012 through FY-2014 as adopted by the Board of Commissioners in September 2011), there will be no uses of General Fund equity that cannot be replaced through employee turnover and / or other favorable variances in that year, reservations of encumbrances and subsequently appropriated carry-forward amounts. The planned growth in the General Fund equity has arisen to cover the roughly \$116.2 million in cumulative operating shortfalls anticipated through FY-2015.
- **GASB Pronouncement.** Effective with the closing of the accounting records as of September 30, 2011, new Government Accounting Standards Board (GASB) rules requiring the County to eliminate several funds by transferring the equity into the General Fund. For several funds (CCIRF for example), this simply accelerated the transfer originally contemplated for FY-2012. An adjustment to relieve the FY-2013 operating budget for the effects of this requirement was made in the Summary Schedule. In other instances (Land Sales Fund, for example), there had been no budgetary intention to transfer this equity into the General Fund. Accordingly, the required transfer of these funds into the equity of the General Fund appears to have increased the General Fund equity without actually increasing the available assets to the County. Adjustments have been made to the Framework presentation for these operations affected and the presentation has been adjusted to reflect the general independence of these funds' operations, as discussed subsequently.

During FY-2011, the Printing, Mailroom and Convenience Copier Fund was eliminated. Printing services were largely outsourced to the Oakland Schools. The mailroom is being treated as a central service function billed via the indirect cost allocation. The convenience copier activity was transferred to the Information Technology Fund. Because the print shop was experiencing operating losses, the remaining \$45,000 in this Fund should have been transferred to the Information Technology Fund. However, in error, the \$45,000 was transferred to the General Fund. This matter will be corrected in the first quarterly report for FY-2012.

Bloomfield Park – The Bloomfield Park development project (located on Telegraph Road just north of Square Lake Road) feel victim to Michigan's 10-year recession and the project fell into bankruptcy. If there comes a time that the property taxes are not paid,

the title to the property may revert to the County's Treasurer. If that happens, it is possible that there will be an adverse fiscal impact on the County. Steps are being taken to make this outcome unlikely. Nevertheless, it is to be noted that there is no appropriation contemplated in this Framework for an adverse outcome. The Framework assumes that this project will not require any future County resources as a tax foreclosure is not presently imminent.

- **Pontiac.** Under Act 4, the emergency manager is actively restructuring the City of Pontiac's operations and has actively involved the County for the first time in helping to solve these fiscal issues. Any absorption of City operations by the County is assumed to occur only with the full cost recovery.
- **Inflation.** Inflation projections (other than healthcare) are modest. However, recent events in the Middle East involving oil (e.g. gas prices), food shortages and the federal government's monetary policies could result in inflation above the assumptions used. If so, labor and vendors would be expected to attempt to secure commensurate compensation increases to cover the inflation levels then occurring. Property tax revenues are capped at 5.0% for inflation – leaving expenditures to exert inflationary pressures against a capped revenue base. No provision has been made in this analysis for the return of inflation seen in the mid to late 1970s.

A fair amount of the FY-2014 operating shortfall arises from the fact that the operating departments have not yet structurally reduced operations by an amount sufficient to insure they operate within the revenues available for FY-2014 and beyond. To date, the operating departments were only tasked to solve the operating shortfalls through FY-2014. FY-2015 actions are under consideration in this Framework report.

While other assumptions exist throughout the entire budget, the above listing represents the most critical assumptions in understanding the proposed Framework for the operating budgets for FY-2012 through FY-2015.

ASSESSMENT OF BUDGET TARGETS – PRIOR FRAMEWORK DOCUMENT

The last Framework document was issued on March 2, 2011. It set targets for County operations supported by the General Fund or otherwise impacting the General Fund, documented budget risks, and described how the County could successfully pass operating budgets for FY-2012 through FY-2014 and maintain appropriate equity targets at September 30, 2014. The County Executive's recommended operating budget incorporated recommendations and plans developed jointly by the Executive and county-wide elected officials and the plan was passed by the Board of Commissioners in late September 2011. With the closing of the accounting records as of September 30, 2011 the County needs to re-benchmark the early budgetary assumptions as more current information is now available.

The County will use \$17,508,000, \$39,083,000, \$45,817,000 and \$13,754,000 in General Fund equity as of September 30, 2011 during the FY-2012 through FY-2015 (as adopted by the Board of Commissioners in September 2011), respectively. **The General Fund equity of \$201,162,000 at September 30, 2011 will be reduced through the use of \$116,162,000 of equity over a four-year period**, assuming that operating departments adhere to prior commitments and projected central tasks culminate in realized net savings.

The structural operating issues relating to the FY-2016 period of \$46.4 million remain largely unaddressed – except to the extent of anticipated restructuring of County operations yet undertaken. The equity was increased over the past several years in a planned manner to accommodate these anticipated operating shortfalls – leaving an acceptable level of equity in the General Fund and all related operating funds that impact the General Fund.

Unfortunately, some governments use equity alone to ‘solve’ their immediate operating needs without considering any future operations an approach that makes sense only if the causes of the operating shortfalls are temporary and economic recovery is relatively assured in the near future. However, it is clear now that Michigan governments’ operating shortfalls are not temporary and economic recovery cannot be expected in the near term. Long ago Oakland County recognized the need for permanent restructuring and has taken actions within operating departments to address its fiscal issues.

Despite federal and state programs attempting to lower it, the State’s unemployment remains high at just under 11.1%. University of Michigan economists indicated that Oakland County lost 60,000 jobs in 2009, and predict, even with the modest growth, it will take three years to restore *one-half* of the jobs lost in 2009 alone. They indicate that the complete replacement of jobs lost since 2002 will take a very long time. This position by the University of Michigan economists likely means that any significant property tax revenue growth beyond inflation is unlikely for the next decade. Further revenue issues are presented by the fact that the national and State governments have unresolved structural operating shortfalls that cannot be allowed to continue. Any actions taken to remediate those fiscal problems will likely have adverse impacts on local units’ revenues and thus, programs.

There is nothing on the economic horizon that suggests that the current revenue base (and particularly property tax revenues) will return to pre-2007 historical levels any time soon. Given the economists’ projections that a sustained recovery will be at least a decade out, it is clear that use of equity alone or as the primary means to cover revenue shortfalls is fiscally dangerous. Use of equity, without a long-term financial plan and without controls to ensure that the plan is met, will likely result in some local units of government falling into Act 4 where an emergency manager is appointed to run the local unit. Oakland County has both a plan and controls to ensure that this pitfall will be avoided.

It seems clear that many governments cannot secure the political will to reform and resort to the use of equity as a stop-gap measure. Equity can be used only once; equity is directly related to liquidity as the principal asset in the funds described in this section of the Framework. Cash

needed to pay payrolls, fringe benefits and vendors. Deficits mean a deficiency in cash; jeopardizing the ability to pay normal operating costs and often a need to address cash flows 'holes' occurs in a crisis mode – adversely affecting services to the public.

On the other hand, structural, operating reforms benefit the current year and each succeeding year if structural. Oakland County's judicious use of equity, its political will to reform and its adherence to a long-range fiscal plan enables the County to responsibly use limited amounts of actual equity as reflected in the prior year's comprehensive annual financial report accumulated in excess of future targeted amounts to maintain a base of stable services as the operating departments continue to implement more efficient methods for service delivery.

The use of equity accumulated in excess of targets to maintain stable service levels requires a delicate balancing act – if one reduces equity too far without replacement or structurally changing operations, the entity may enter a declining operating spiral (and may experience an insufficiency of cash for operations). Short-term borrowing may be required to maintain operations and interest costs then further exacerbate the downward spiral. The borrowed cash gives elected officials comfort that this can be continued indefinitely even as the deficits mount to a point where the entity may face the State imposition of an emergency manager. Borrowing cash used to be easy; repayment of the borrowed money when fiscally distressed and in the absence of political will to address prior operating issues is difficult.

The retention of excess equity without specific plans in its operating use burdens taxpayers and would be inappropriate. Oakland County's delicate balancing efforts of addressing cash needs while retaining sufficient equity to cover future shortfalls and while maintaining equity to meet the goals discussed earlier, especially that of stable services to the public, all without retaining too much equity has been successfully accomplished for years. Key to this accomplishment has been the cooperation and support of the County-wide elected officials. The expectation of this cooperation continuing is one of the assumptions contained in this Framework document.

In addition to the General Fund, several other funds assist the County's General Fund in providing service support (internal service funds billing the General Fund, for example) or transfers into the General Fund (Delinquent Tax Revolving Fund, for example). The equity targets for these other funds must be reviewed and set during this process, to avoid the possibility that the General Fund's equity is controlled at the expense of deficits created in other County funds (a clearly unacceptable practice common in fiscally distressed entities).

The funds indicated in this section cite the anticipated reductions in equity and related targets as of September 30, 2011 and leveling off afterwards to the targeted equity levels as of September 30, 2015. The County's adopted operating budget for FY-2012 through FY-2014 (based on the March 3, 2011 Framework) contemplates the use of equity accumulated in excess of targets, and thus, **already realized** as of September 30, 2011. The excess equity over targeted amounts is used ratably over the three-year period to minimize operating impacts in the current year or for the operating shortfall in the next year in its entirety.

This approach provides a ‘smoothing’ of the use of accumulated equity in excess of targets and allows for portions of equity to be used in the second and third years out, thereby providing a cushion against any significant unanticipated fiscal events as well as time to restructure County government. Employee reductions have thereby occurred largely by attrition instead of through involuntary separation. Other operating crises are also averted.

As cited in the Framework of several years ago, the County’s “accumulated equity in excess of targets tool” assists in solving the fiscal issues facing the County in the near term, but it has a limited life span associated with it: at the end of September 30, 2012, all equity already accumulated in excess of targets as of September 30, 2009, was depleted down to the targets as expressed in the 2010 Framework document (assuming, of course, that the prior projections today hold true). For example, the Jail Population Fund and CCIRF Fund anticipated the ratable use of equity for the periods FY-2010 through FY-2012, down to the full liquidation of these Funds.

Therefore, reliance on the operating transfers in for future years is no longer possible – the Fund, cash and equity have been moved into the General Fund to support prior operating needs. After the significant growth of the General Fund equity through September 30, 2011, most operating shortfalls after FY-2015 will rely heavily on reductions in operations. The County has several years to restructure its operations under the current economic assumptions expressed herein.

This section addresses the County’s General Fund and operating funds that are highly dependent on the General Fund for resources or would be able to provide resources to the General Fund. The equity targets cited in the prior year must be addressed if less than the target and / or equity in excess of the targets created in FY-2011 would serve to assist in mitigating the operating shortfalls through FY-2015.

General Fund

As reflected in the prior year’s Framework, the equity target for the General Fund as of September 30, 2014 is \$85.0 million. The same equity target is used here for September 30, 2015 as it continues to represent approximately 20% of projected FY-2015 expenditures.

As reflected in the Summary Schedule, the General Fund equity as of September 30, 2011 is the starting point for the determination of the cumulative operating shortfalls for the periods FY-2012 through FY-2015 before considering central and operating department budget tasks, if necessary. The ending equity in the General Fund is higher than originally estimated for the following reasons:

- The most significant reason why the equity position is up is that the restructuring of various departmental operations, the hiring freeze, limitations on capital outlay, and the initiation of new projects and actions by operating departments voluntarily controlling spending allowed for equity to increase.

- The Governmental Accounting Standards Board Statement No. 54 mandated that several funds previously classified as special revenue funds be moved into the General Fund including: the CCIRF Fund (budgeted in FY-2012 to be closed into the General Fund anyway - \$8,119,000 and Land Sales Fund (actual closed restricted balance - \$3,541,000).
- The County reversed \$4.85 million in liabilities set up for Michigan Tax Tribunal (MTT) cases based on an analysis as of September 30, 2011 and the related future exposures. Two matters are occurring: first, as the cases linger in the MTT the value of the properties has declined and thereby reduce the dollar exposure to retroactive claims; and second, the cases are clearing and being recorded in revenue - thereby reducing revenue, now offset by the reversal of the liability back into operations.
- The original budget predicted a decline in the December 31, 2010 assessment roll of 9.0%; the actual decline came in at 7.78%, resulting in additional property tax revenue favorability.
- Unlike others, the County used little of its equity as of September 30, 2010 during FY-2011, meaning the small amounts to be replaced were available as a result of employee turnover and other favorable variances. Said another way, the favorable variances arising from responsible operating department management served to increase the equity levels beyond the original targets.
- Included in the equity is \$5.4 million of carry-forward equity arising from favorable variances and / or programs where the amounts were not expended but the revenue recognized. The amounts have been proposed to be reappropriated in the December 2011 Board of Commissioners meeting and are anticipated to be spent in FY-2012. The most significant amount arises from the State receivable involving the Convention Facility Development Fund as the State continues to delay its payment (paid by the State in very late October 2011 for FY – 2011 operations). These revenues are used for substance abuse (50%) and a General Fund discretionary distribution from the State (50%). County management has been instructed not to spend the funds until they are received from the State.

Revenue Sharing Reserve Fund (RSRF)

During fiscal 2005, the State revised the property tax calendars for counties and it created a substantial and permanent future cash flow hole for virtually all Michigan counties lasting from December 1 to June 30th each year. Oakland has yet to experience this cash flow hole as its Revenue Sharing Reserve Fund (RSRF). The RSRF was created by the State-mandated collection of a full year's property taxes over a three year period is yet to be exhausted.

By law, this fund is to be drawn down at a pace of now \$24 million annually as a means to “cover” the annual revenue sharing payment that the State no longer makes to Oakland County. The State Treasurer sets the amount of operating transfers out of the RSRF. By 2013, the amount of cash in the RSRF will begin to be insufficient to compensate for the cash flow hole in the General Fund during certain parts of the year (likely March through July). As such, the County may be required to borrow to cover payrolls and vendor payments then due in the spring and early summer 2013, but certainly no later than FY-2014. The estimated interest costs for the anticipation notes to be issued has been included in the FY-2013 and beyond operating budgets.

Over the past several years, during June and July periods, Oakland County has seen the General Fund experience a ‘negative’ cash position that has amounted to over \$80 million in FY-2009. This cash-flow hole exists even when the General Fund ‘positive’ equity is in a surplus position. Currently, the cash-flow hole is covered by borrowing from funds that have yet to be drawn down in the RSRF. The RSRF is paid back before year’s end when the proceeds from the annual tax levy are realized. Starting in FY-2015 when the RSRF is completely eliminated, there will be a need to borrow from outside County funds (e.g. banks). The amount borrowed could be as high as \$75 million to \$100 million for certain months of the year, adding new interest charges to the cost of County business.

Nevertheless, it is believed that the thoughtful position of using equity accumulated in excess targets cited herein, coupled with real operating reforms and structural changes should allow Oakland County to retain its AAA bond rating. In doing so, the County can mitigate its interest costs starting in FY-2013 due to the annual borrowing necessitated by the state-imposed changes in the property tax collection calendar. By September 30, 2014, the estimated equity for the Oakland County’s RSRF will be \$11 million to be used in FY-2015.

With the changes in statutory revenue sharing imposed by the State this past spring, those counties where the RSRF were already exhausted and thus are again receiving statutory revenue sharing took a one-third reduction in the revenue sharing for FY-2012 over FY-2011 levels. The reduction is expected to be permanent. Given this fact, County administration believes that when the County again begins receiving revenue sharing in FY-2015, it is highly unlikely that it will secure more than a two-thirds level of payments based on the \$24 million previously provided under the RSRF, or roughly \$16 million in revenue sharing revenue for FY-2015. Given the carry-over of \$11 million in RSRF from FY-2014, the State would be expected to supplement the County’s shortfall in revenue sharing by \$5 million. The one-third reduction in revenue sharing has been reflected in the FY-2015 operating shortfall.

Interim Retirees’ Medical Benefit Trust (Interim Trust) / VEBA

The County has two funds that operate to fund the retirees’ healthcare program as follows:

- Interim Retirees’ Medical Trust – the fund has retained the proceeds of the original certificates of participation (COPS) with two purposes: providing the annual required

contribution to the VEBA as recommended by the County's actuary and hold the funds in the event of an adverse national or state healthcare policy such that the COPS would be defeased quickly, if necessary to protect the County's interests.

- VEBA – the VEBA receives the annual required contribution from the Interim Trust and pays the retirees' benefits when due.

Annually, the Fringe Benefit Fund collects funds from the operating departments sufficient to cover the debt service on the COPS.

A quick assessment of the status of the County's retirees' healthcare program follows:

- The combined net assets at market value as of September 30, 2011 are \$835.7 million (\$544.7 million in VEBA and \$291.0 million in Interim Trust).
- The latest actuarial report is September 30, 2010 (such report is normally issued in spring of the following year; in this case March 28, 2011). The actuarial report cites that the total obligation due and earned by employees through that date is \$794.1 million.
- While a direct comparison is difficult at this time, since the County has been actuarially funding the plan for years and the payments from the VEBA have remained relatively constant, the comparison would be warranted at this time. In doing so, the County's indicated financial position is that the retirees' healthcare program remains fully funded with an excess of assets over obligations of roughly \$41.6 million (\$835.7M minus \$794.1M).

The annual required contribution of \$37.3 million, which has been reflected in the operating budgets for FY-2012 through FY-2014 as adopted, could increase over time. However, the point at which the originally developed model would suggest a funding necessity from the General Fund when the COPS were issued in July 2007 is \$60.2 million. It is highly unlikely that the annual required contribution could grow from the current FY-2012 levels to an amount in excess of \$60.2 million over the period through FY-2015. Accordingly, at this time, the retirees' healthcare program is functioning as originally anticipated in July 2007 (when the COPS were issued) and no further analysis is required in this interim Framework report.

A detailed analysis of the financial condition of the Interim Trust and VEBA in support of the retirees' healthcare system will be evaluated in the final Framework document.

Delinquent Personal Tax Administration Fund

The Delinquent Personal Tax Administration has \$2.8 million in equity as of September 30, 2011. The equity target for September 30, 2012 is \$1.0 million, with ratable reductions included in the adopted operating budgets for 2012 of \$1,691,000 (third year of a three year

programmed reduction). Under this originally-set target, this Fund would have \$1.1 million in equity as of September 30, 2012. No adjustment to the Summary Schedule is warranted.

Property Tax Forfeiture (Land Sales) Fund

In accordance with GASB Statement No. 54, the Land Sales Fund equity was moved into the General Fund. Of the \$4,083,000 in equity, \$3,541,000 is restricted and unavailable for the general operating purposes of the General Fund. The remaining amounts would be available.

The equity position before transfer was well above the anticipated equity position in the spring Framework for several reasons:

- The summer auctions resulted in revenues above the expectations in the operating budget.
- Several of the properties expected to be demolished last year were moved into the federal NSP-2 grants.

Because the former Land Sales Fund operations have now been reflected in General Fund equity, no further consideration of the operations are necessary unless the full restricted and unrestricted equity position is fully expended and creates reductions of General Fund equity in future periods.

Capital and Cooperative Initiative Revolving Fund (CCIRF)

As discussed in the spring 2009 Framework document, the CCIRF was to be eliminated over a three-year period of time starting FY-2010 and ending FY-2012. Because of GASB Statement No. 54, the ending equity in this separate Fund as of September 30, 2011 was moved into the General Fund one year earlier than originally budgeted.

Jail Population Fund

The Jail Population Fund is the only Fund where the equity is being used over a two-year period of time. The equity balance as of September 30, 2009 is \$2.8 million with a \$1.4 million transfer into the General Fund for FY-2010 (already transferred last year) and FY-2011, at which time the Fund was closed.

Delinquent Tax Revolving Fund (DTRF)

Over the past several years, the County has judiciously used the DTRF operating surplus to fund certain General Fund operating costs. The DTRF operations have been used to fund debt service payments, the Tri-Party program (now shifted to the General Fund equity for support in FY-2011 and beyond), and other General Fund operations at an historic operating subsidy level of \$7.1 million.

In addition to the DTRF's primary purpose of factoring delinquent real property taxes receivable from local units of government (including those delinquent taxes applicable to the General and Parks and Recreation Funds), the DTRF has become an important tool to assist in the support of General Fund operations and related programs – and mitigate deeper cuts by County operating departments while restructuring is underway.

Recently, the equity position of the Fund has increased slightly beyond targeted amount of \$200 million longer term because of increased penalties and interest that come with the rising property tax delinquencies resulting from the problems in the real estate and employment markets.

In recent years, the Fund has borrowed short-term notes in order to insure sufficient resources to factor the delinquent tax receivables due to local units of government each spring. Delinquent taxes are expected to remain somewhat higher than historical levels given the condition of the real estate market in southeastern Michigan, unemployment rates and the slow recovery of the economy. The recent annual purchases of delinquent real property taxes have approximated \$160 million; annual amounts borrowed have been in the order of \$50 million, with the rest funded from the existing liquid resources within the DTRF.

In addition to the operations cited above, the County refinanced several debt issues that are being funded out of the DTRF operations. Savings have resulted from these debt defeasances as well.

The target DTRF equity was set at \$200 million as of September 30, 2012, and beyond. At September 30, 2011, the ending equity was \$218.7 million (approximately \$3.7 million higher than the March 2011 Framework projections). The FY-2012 operating transfers to support the General Fund as reflected in the adopted operating budget was \$23.15 million, respectively; with a \$9.1 million operating transfer to the General Fund from the DTRF in FY-2013 and FY-2014. The DTRF experienced a planned reduction of \$6.3 million in equity during FY-2011. Additional reductions are expected in FY-2012 and beyond.

The real estate market remains stressed. The unemployment rate remains stubbornly high. Mortgage and tax foreclosures for calendar 2010 are at near record levels of 9,242. Calendar 2011 mortgage foreclosures are estimated at 7,500. These conditions indicate there will be increasing investment income against the adopted operating budgets and together with the debt defeasances, DTRF levels will support increased distributions for FY-2013 and 2014 from the historical level of \$7.1 million to \$9.1 million; such amounts were included in the operating budgets approved by the Board of Commissioners.

The DTRF long-range projections for the Wall Street presentation will be completed in winter 2012 during the preparation of an updated Framework by the Department of Management and Budget in cooperation with the Treasurer's Office. This preliminary review suggests that the DTRF remains healthy and capable, with appropriate borrowings, of factoring delinquent real

property taxes on behalf of local units of government. The Summary Schedule has not been adjusted for any amounts applicable to the DTRF at this time.

Facilities Maintenance and Operations Fund (FM&O Fund) / Building Improvements Fund

There are two facilities-related Funds in operation in the County:

- Facilities Maintenance & Operation (FM&O) Fund – covers the operations of the facilities, maintenance and related costs with amounts billed back to the operating departments by building on a square footage basis.
- Building Improvements Fund – covers the major maintenance related items (roof, HVAC, paving, etc.) on a project by project basis. This Fund’s operation is often referred to as the “Capital Improvement Program.” The projects are funded as needed from a variety of sources – General Fund subsidies, grants, bonds, etc.

In connection with the adoption of the FY-2011 through FY-2013 operating budgets, the rates for the FM&O Fund were reduced to bring the equity from the \$10.9 million at September 30, 2010 down to roughly \$8.0 million as of September 30, 2012. At September 30, 2011, the ending equity was \$12.2 million, in large part due to favorable variances in electricity, heating and other related operating costs by the FM&O Department. The Fund also fared better than expected during the current year. The FY-2012 year has a planned equity use of \$1,345,000 as adopted in the operating budget by the Board of Commissioners.

While slightly higher than anticipated arising from FY-2012 operations, the FM&O Fund is not recommended for any adjustments given the likely need to address deferred maintenance issues and an equity position in the Building Improvement Fund lower than a reasonable level of equity should be for major capital maintenance. The ending equity of the Building Improvement Fund was \$9.5 million (earlier projections suggested \$8.9 million in the capital improvement program adopted by the Board of Commissioners in the summer of 2011). While sizable, this Fund anticipates the use of equity such that the ending equity will decline to \$680,000 by September 30, 2015 – too low to provide any reasonable major maintenance items.

However, between these two Funds, the County’s capital needs over the next several years are considered to be adequate. As a cushion against any unanticipated needs, the General Fund has set aside \$9.0 million in assigned equity as of September 30, 2011. But, the use of this equity component is to be considered a last resort as it would place pressures on the equity target of the General Fund now set at \$85 million – only to effectively create a budget task for operating departments if used.

The County anticipated the sale of the west Oakland County office building but the original buyer is no longer interested. The net sales revenue expected to be contributed to the FM&O

Fund from this sale were to be roughly \$250,000. No Summary Schedule adjustment is needed as it was not formally incorporated in the operating budget as a sale was never consummated..

The facility and related needs will be reviewed over the next several months. These operations may be revised in the final Framework report for the periods FY-2012 through FY-2015 when more information is available.

Information Technology Fund

The Information Technology (IT) Fund has an unreserved equity as of September 30, 2011 of \$11.4 million with another \$4.9 million designated. The most significant issue facing the Fund is the ultimate replacement of existing equipment with a cost of \$57.7 million and accumulated depreciation (essentially an indication of the used up component of the equipment) of \$50.6 million – leaving only \$7.1 million of remaining value. Total equity represents both unreserved / reserved and the net book value of equipment is \$23.4 million. The Fund equity is represented in a cash position of \$16.3 million and working capital (liquid assets less amounts owed at year end) of \$16.3 million. The Fund’s immediate liquid position is in good shape; the longer term solution of future capital needs has to be addressed.

Replacement costs of computer equipment routinely decline over the years from the time of the original purchase to its replacement. However, it is unlikely that the equipment cost today would have declined as much as it would be required to replace it within the existing IT Fund resources. The capital needs of the IT Fund to be obtained via operations or General Fund support (see subsequent discussions for transfer in future years) will have to be stabilized as part of the assessment during the next round of strategic planning efforts for the Fund. Helping to stabilize this Fund’s financial condition (even as it is creating some operating issues) are the vacancies of between 20 to 30 positions over the past year or so.

It should be noted that \$5.0 million of General Fund equity has been set assigned for the replacement of the equipment but the use of this equity component is to be considered a last resort as it would place pressures on the General Fund equity target. Provisions for \$1.5 million, \$3.0 million and \$3.0 million for the FY-2013, 2014 and 2015 operating budgets, respectively, have been reflected in the Summary Schedule to cover a modest amount of equipment replacements.

Two other matters of note follow:

- The Information Technology Fund has recently experienced a higher than expected turnover with a difficulty in securing replacements. The information technology market for employees is highly competitive in this region and a number of County employees have left to move to the private sector. Presently, there are approximately 30 vacant positions in this Fund.

- During FY-2011, the Equipment Fund was closed to the Information Technology Fund and the remaining equity of \$3.1 million transferred as well.

Building and Liability Fund

The Building and Liability Fund provides for losses in claims, litigation and / or assessments. Prior years' Framework reports cited a target of \$15.0 million for equity as of September 30, 2012 and beyond, with annual reductions in rates billed to County funds in FY-2010 through FY-2012 to move the then equity down to that level. The Fund's equity at September 30, 2011 is \$17.9 million, with an excess of revenues over expenses of \$2.0 million occurring in FY-2011.

The Fund equity is slightly higher than the target set several years ago. The Fund broke even in FY-2010 and showed an excess of revenues over expenses in FY-2011 of \$2.0 million. The acceptance of the City of Pontiac Sheriff's patrol contract on August 1, 2011 may present a higher likelihood of loss than that experienced in other law enforcement contract communities. To date, however, outside the Loss Reserve and Forecast Analysis report prepared by Aon Risk Consulting for Oakland County on October 17, 2011, there is no loss experience to formally cite in this report. Accordingly, County administration estimates that this Fund's financial condition is currently adequate. The Fund levels will be reviewed again in the spring 2011 in connection with the formal preparation of the operating budgets for FY-2013, 2014, and 2015. No adjustment to the Summary Schedule is warranted at this time.

Fringe Benefit Fund

The Fringe Benefit Fund equity was \$12 million as of September 30, 2009 and September 30, 2010, remaining relatively unchanged. In FY-2010, \$135.65 million in revenues / expenses flowed through this Fund. The Government Finance Officers Association suggests that operating funds maintain two months of equity – roughly 16.7% when compared to revenues (or, upwards of \$22 million in equity). At present, this Fund has less than 10% against the GFOA standard. The actual results in the past have resulted in a need to increase equity during FY-2011 and beyond to provide sufficient working capital for operations. As of September 30, 2011, the ending equity was \$19.0 million with expenses of \$131.6 million, or 14.4%, a more acceptable level of equity.

As noted previously, there are a number of uncontrollable factors impacting the County's fringe benefits that must be considered in the future as real information becomes available: federal healthcare changes; Public Act 152 (80 / 20 split or Caps on healthcare); loss of grandfather status in healthcare; deputies Act 312 award expected in the winter of 2012; general inflation; etc. This entire area requires close scrutiny over the next several years.

The Fund's projections have been difficult to develop as the hiring freeze, restructuring of operations (and thereby reducing of employees), and use of part-time, non-eligible employees in lieu of full-time employees result in significant shifts of billed charges to the operating funds. With much of the Fund's operations being fixed in the form of debt service for the retirees'

healthcare debt service, as the base of salaries and employees charged declines, the fringe benefit charges to operating funds vary radically – even as some costs remain unchanged.

The adopted budget for the active employees' healthcare costs (medical, eye care, dental, etc.) for FY-2012 through FY-2015 was projected to increase annually at a pace of 6.0% for the next four years. The actual results for FY-2011 would suggest otherwise. The Summary Schedule for FY-2012 through FY-2015 arises from a lowering of the projected cost increase to roughly half of the originally anticipated increase effective January 1, 2012. The rates will be adjusted effective January 1, 2012 as well when billings to operating funds occur from employee service.

Motor Pool Fund

Over the past half dozen years, the Motor Pool Fund received roughly \$2.0 million in working capital as the rates charged to operating departments were insufficient to cover operating costs. About two years ago, the rate structures were revised. The newly adopted rate structure stabilized the annual revenues for the Motor Pool Fund and provided too much revenue relative to the operating and capital needs over the next several years. Accordingly, during FY-2011, the Fund returned \$750,000 to the General Fund in the third quarterly report.

As of September 30, 2011, the Fund has \$3.5 million in equity and that amount is backed largely by cash – meaning the fund has the liquidity necessary to acquire vehicles. Over the past several years the Fund has needed roughly \$2.2 million to \$2.5 million in annual available cash to cover the routine replacement of vehicles. Given the equity position, cash available now after restructuring the rates billed to operating departments and the capital program into FY-2012, the Summary Schedule has projected the return of \$500,000 of the working capital provided in prior years (a 'one-time' return). With the return, the Fund will still have adequate resources to cover FY-2012 capital needs and operations.

FOOTNOTES TO SUMMARY OF FUTURE OPERATING ISSUES AND SHORTFALLS – GENERAL FUND SCHEDULE

The footnote references included on the "Summary of Future Operating Issues / Shortfalls – General Fund" (Summary Schedule) are explained.

The adopted triennial plan for Oakland County reflects critical central budget reductions and departmental budget tasks that were undertaken and completed by operating departments during FY-2011 and prior years. The County started its restructuring as early as FY-2002 and the actions undertaken to date have served to mitigate what other local units of government are struggling to address today – often as these units are in deficit (liabilities > assets). The restructuring of departmental operations were particularly aggressive in the FY-2009 and FY-2010 periods.

Generally, County departments restructured operations early in order to meet the budget tasks assigned. As of September 30, 2011, these early departmental actions have provided additional

General Fund equity over targets, thereby serving to reduce future budget tasks that otherwise would have needed to be assigned in order to balance the FY-2015 operating budget.

Combined with restrictions on hiring, on new capital projects and on any significant large investments (without superior returns on investment), the FY-2011 and prior departmental budget reductions have placed the County on solid fiscal footing going forward. Both Standard & Poors and Moody's Investor Services recognized the control and reduction efforts and continued to reward Oakland County with AAA bond ratings for its recent refinanced debt, just one outside example of the benefits of long-term financial planning.

Note A - Appropriated Budget

The General Fund revenues and expenditures for FY-2012 through FY-2015 have been extracted from the operating budget adopted by the Board of Commissioners in late September 2011. Beginning with the recently passed operating budget, the operating shortfalls for FY-2015 and FY-2016, which are summarized at a County-wide level, will be updated with each resolution now being passed, if applicable. This will continue to highlight the continued structural operating shortfall for the farthest year out – now FY-2015.

Because of the early actions by operating departments, the County successfully closed its accounting records for FY-2011 with a General Fund equity position above that which was projected in the spring 2011 Framework. As cited previously, this additional equity position benefits the FY-2015 period and results in a lower budget tasks for operating departments going forward.

A presentation of the recommended budget for FY-2012 through FY-2014 periods was provided by the County Executive in July 2011 to the Board of Commissioners. At that time, the projected ending equity position of the General Fund was \$155.9 million based on the second quarterly close in FY-2011. The actual closed General Fund equity (unaudited) as of September 30, 2011 was \$201.2 million, for a difference of \$45.3 million. As already noted, the differences were largely the recognition of two quarter's additional turnover favorability, GASB mandated transfers of various funds (CCRIF and Land Sales Fund, for example) into the General Fund that were not contemplated for FY-2011, a settlement with the State in a rate dispute, return of operating funds from the Motor Pool Fund and other related benefits not known and accounted for in the previous budget.

The higher General Fund equity as of September 30, 2011 benefits the projected ending equity at September 30, 2015 allow for stable delivery of critical services to County residents and mitigates the need to impose interim budget tasks on County operating departments.

Note B - Pension Contributions

Exhibit A projects the pension contributions anticipated between now and FY-2015. It is based on the actuarial report received in spring 2011, on the investment performance for FY-2011,

and on the ending market value of the investment portfolio as of September 30, 2011. In the December 2010 Framework, the pension contributions for the defined benefit plan for FY-2012 and beyond were estimated at \$5.0 million and were included in the adopted budget passed in September 2010. The projection was based on a three-year smoothing of investment gains and losses. An actuarial report issued in February 2011 using the three-year smoothing recommended the following contributions for FY-2012:

- General Employee Pool - \$119,041 (2.25% of total contribution).
- Sheriff Command Employee Pool - \$1,994,291 (38.0% of total contribution).
- Sheriff Deputy Employee pool - \$3,141,633 (59.75% of total contribution).
- Total Contribution - \$5,254,965. (The 2010 Framework estimated \$5.0 million a year earlier).

Pension contributions for the Sheriff Command and Deputy Pools prior to this year have been covered by the excess assets in the General Employee Pool so no pension contributions from the County General Fund were required to cover the shortfalls in those pools. Because of smoothing, the impacts on pension contributions caused by the significant investment losses during the national recession in FY-2008 and FY-2009 were not estimated to have a funding impact until FY-2012. This is because when using the three-year investment smoothing, all three employee pools had an excess of liabilities over assets. However, it was clear that in FY-2012, because of the investment losses, the internal transfers between pools could not occur and the County was going to be obligated to fund the pension contribution if the three-year smoothing practice was continued.

During the spring Framework preparation process, the County reviewed the policy of smoothing investment gains and losses over a three-year period and decided to change the policy to a five-year period, a practice authorized by actuarial standards and when disclosed in the financial statements, acceptable under the Governmental Accounting Standards Board principles as well. By adopting this practice, projected required contributions were eliminated for FY-2012 and FY-2013 and only a \$602,000 contribution would be required in FY-2014.

The revised spring Framework projections for pension contributions provided for a modest growth in the investment portfolio based on events in the late 2010 calendar year and winter of 2011. Unfortunately, this growth was not fully realized as a number of adverse international events occurred (e.g. Greece and other countries' fiscal distress; the overthrow of certain Middle East leaders; the continuing lagging economy and a lack of improvement in the unemployment rate; etc.). As a result, the defined benefit pension plan investment portfolio as of September 30, 2011 was well below original projections. In addition, the pace of County retirements picked up and the amount of benefits required to be paid were higher than estimated.

Accordingly, the pension contribution projections expressed in Exhibit A have been prepared with the known investment gains and losses included. They will be smoothed over a five-year term rather than a three-year term. Based on the lower level of investments as of September

30, 2011 and the continued market volatility, the portfolio is expected to grow by roughly 3.0% to 3.5% annually through September 30, 2014. The County has a substantial number of employees that have the capability to retire in the next several years and they may do so. Some will have their final average compensation being reduced, in part, by the salary reductions taken over the past several years.

Comments follow on Exhibit A (which follows the formulas used in determining the pension contributions, including investment smoothing for gains and losses in the investment transactions):

- All assumptions used in spring 2011 actuarial report remain unchanged (final average compensation factor, turnover, life expectancy, etc.).
- Once the other assumptions are held constant, there are only three significant inputs into the schedule that affect the pension contributions – the rest of the schedule follows the formulas used by the County’s actuarial firm:
 - **Investments – Market Value at Year End.** The market value of investments at September 30, 2011 was used in the calculation of the net assets in the defined benefit pension plan. The portfolio is expected to increase by 3.0% to 3.5% over the next several years.
 - **Cash Flow.** The cash flow is largely the pension payments to retirees and administrative costs. Given the recent incentive program in the recent past, the cash flow has been increased to reflect the increased level of recent retirees.
 - **PV of Future Benefits.** The present value of the future benefits has been reflected at a modest 1.5% growth rate.

Exhibit A reflects an anticipated contribution for the following years – using the five-year investment gain and loss smoothing:

- FY-2012 – None.
- FY-2013 - \$960,260.
- FY-2014 - \$2,311,851.
- FY-2015 - \$3,965,854.

Based on the status of the contributions and related pools developed above expressed in the February 2011 actuarial report, the required contributions are almost certainly because the underlying three employee pools have an excess of liabilities over assets. Assuming that the relationship remains relatively unchanged, then just 2.25% of the contributions above would relate to the general employee pool and the remaining 97.5% would be attributed to the Sheriff’s Office personnel, or \$24,007, \$57,796, and \$99,146 for FY-2013, FY-2014, and FY-2015,

respectively for the General Employee Pool. The net amounts attributed to the Sheriff's Office personnel would be \$936,253, \$2,254,055, and \$3,866,708 for FY-2013, FY-2014 and FY-2015, respectively.

Roughly 75% of County employees work in the General Fund operations. As such, \$18,004, \$43,347, and \$74,359 for FY-2013, FY-2014 and FY-2015, respectively, of the general employee pools' required contribution would be attributed to the General Fund. When combined with the Sheriff's Office required contribution, the amount to be included on the Summary Schedule follows:

- FY-2012 – None.
- FY-2013 - \$954,257 (\$18,004 + \$936,253).
- FY-2014 - \$2,297,402 (\$43,347 + \$2,254,055).
- FY-2015 - \$3,941,067 (\$74,359 + \$3,866,708).

The pension contribution billed to local units arises because of the inclusion of the above costs in the law enforcement contracts between local units of government and the County as provided by the Sheriff's Office. Presently and through FY-2012, the rates have been developed with no defined benefit pension contribution as the general employee pool has absorbed the amounts otherwise paid by the General Fund up until the time all three employee pools' liabilities exceeded the related assets – at which time the County was required to provide a pension contribution.

The pension contribution cost to be included in the law enforcement rates has some difficulty in its calculation. Issues involved in the allocation of the above pension costs follow:

- There are both defined benefit and defined contribution personnel assigned to the law enforcement contract communities, only the defined benefit pension contribution impact is noted above. Of the contracts (individual deputies) in service, 45 are in the defined benefit plan while 211 are defined contribution (with all of Pontiac's 63 deputies being defined contribution).
- The defined contribution pension costs have only included an amount that is blended – Sheriff's Office and general County employees – charged to all County departments for operations. No defined benefit costs were included as none have been paid since the mid-1990s (defined benefit pension plan was fully funded, even as the Command and Deputy Employee Pools were not, such over-funding arose from the General Employee Pool alone).
- There are two components to the defined benefit costs – 'normal costs' representing the cost of the rights to receive a pension in the future earned in a current period and a provision for the annual cost of the unfunded actuarial accrued liability (UAAL) with the amortization period being upwards of 30 years (e.g. shortage of amounts previously

paid, costs arising from new benefits provided to be paid in the future or actuarial gains and losses arising from differences between the actual results and assumptions).

- The County has and continues to charge a blended pension contribution rate for all employees, even as no formal payment from the County to the defined benefit pension plan was provided. The rate between the deputies / command and general County employees was slightly different with the deputies / command personnel receiving a slightly higher benefit. The pension costs for the command and deputies were covered by the movement *within* the defined pension plan between pools. The rate necessary to cover the defined contribution costs was less than it would have necessarily had to be because the absence of a cost associated with the defined benefit employees, on average, reduced the overall pension costs charged to funds.

The “normal costs” component can easily be developed as it is simply the cost as expressed as a salary percentage as developed by the actuary times the salary of those Sheriff’s Office personnel still in the defined benefit plan. Unfortunately, the current (annual) cost of the “UAAL” component is much more difficult to assign to future rates as it was earned in the past and paid in the future – for the most part without specific services currently being performed. For example, many of the 211 (sans Pontiac) deputies (and command for that matter) who are currently receiving defined contribution pension payments replaced deputies, now on retirement, that were in the defined benefit pension system, but who retired before full funding occurred. Some questions surface:

What costs should be assigned to the future law enforcement contracts for services rendered in the past, but not previously covered in the rates – some components of which would be for recent investment losses and some for other actuarial differences in assumptions?

- Taken to a very logical extreme, if all of the deputies in the defined benefit plan were moved from the law enforcement contracts to other service areas and replaced with defined contribution personnel, would there be no charges burdened on the local units for a simple transfer of personnel – causing the General Fund to absorb the full cost of pension contributions? Essentially in this example the ability to recover costs incurred in prior years or as a result of the recent investment losses would be lost to the detriment of the communities not using law enforcement contracts.
- Should Pontiac be burdened with a higher rate even as they have not contributed to any of the issues as all of the deputies are in the defined contribution plan?

The estimated amount to be recovered by increases in law enforcement contract rates from FY-2012 through FY-2015 is based on the following:

- The portion attributed to the deputies’ component of the pension contribution was allocated based on the patrol salaries in the live product schedule (including funded vacancies) by the total salaries for the deputies. Generally, the deputies are split

roughly between corrective and patrol services with a nominal amount attributed to miscellaneous services, grants, etc. The dollar amount allocated for the deputies is \$271,476, \$653,588, and \$1,121,936 for the FY-2013, FY-2014 and FY-2015, respectively.

- The command (captains, lieutenants and sergeants) positions were added up throughout the department. The number of command staff working in the patrol services to the total number of command staff at these ranks came to \$92,362, \$222,371, and \$381,465, respectively.

The combined amount to be recovered from the added pension contribution has been reflected on the Summary Schedule. The amounts are \$363,838, \$875,959, and \$1,503,401, respectively. The County administration welcomes a further discussion on this matter and any reasonable alternative allocation plan / formula that serves to indicate that the full and direct costs associated with the law enforcement contract rates are being met will be considered.

Note C – GASB No. 5 Accounting Pronouncement: Land Sales Fund and CCIRF

Effective with the closing of the accounting records on September 30, 2011, the Government Accounting Standards Board (GASB) required that funds that are discretionary in their use by local appropriating boards should be reported in the comprehensive annual financial reports as a General Fund operation. The County has several of these operations that were combined into the General Fund in FY-2011 as follows, each with slightly differing impacts on the General Fund and availability to be used in the future:

- **CCIRF** – the Capital and Cooperative Initiative Revolving Fund (CCIRF) had set aside funds in the prior year for the purpose of developing an endowment. When the property taxes and State support declined, the County began winding up operations circa FY-2010 and began moving the residual equity into the General Fund over a three year period from FY-2010 to FY-2012.

Because the CCIRF operations were not controlled by external entities (such as a grant or restricted revenues for a specific purpose), under the new GASB rules it had to be combined with the General Fund in FY-2011 – one year in advance of that contemplated in the appropriated operating budget. As a result, the ending equity in the General Fund as of September 30, 2011 reflects the movement of the CCIRF into the General Fund. Thus, the operating transfer into the General Fund located in the *original* adopted budgets in prior years has been eliminated as the ending General Fund equity at September 30, 2011 reflects not only the FY-2011 operating transfer in but also the collapse of the CCIRF into the General Fund as well.

- **Land Sales Fund** – the Land Sales Fund had transferred unrestricted equity in FY-2010 and FY-2011 in the approximate amount of \$1.0 million annually. Because of the large influx of tax foreclosed homes requiring demolition in the summer of 2010, the County abandoned the originally anticipated transfer in (\$1.0 million) to the General Fund in the

adopted budget by the Board of Commissioners in September 2011. Essentially, the equity position was believed to be needed to cover the demolition costs.

During the two auctions in the summer of FY-2011, the sales proceeds were above the anticipated amounts in the budget, resulting in a more favorable equity position of \$4,083,000 (of which \$3,541,000 is restricted by statutes, with the remaining amount available for use by the General Fund).

Note D – Land Sales Fund – Reverse Planned Use of Equity

The County Executive's operating budget submitted in June 2011 recommended the Land Sales Fund (pre-collapse into the General Fund as noted directly above) would use almost \$1.0 million in equity in order to balance the Fund's operations for FY-2012, FY-2013 and FY-2014. The summer auctions of the tax-foreclosed properties resulted in an increase of proceeds from such sales above any prior levels of sales and the operating budget then adopted.

In the short-term, the Land Sales Fund demolitions costs can be covered by the auction proceeds. Accordingly, the planned use of equity in the short-term will not be needed and has been reduced with an anticipated increase in sales proceeds offsetting the elimination of the use of equity. However, as the real estate market improves over the next several years, the tax-foreclosed properties sold at auction would also be expected to decline – meaning, any backlogged properties requiring demolition may not be covered with auction proceeds circa FY-2014 and beyond. This situation warrants review each year.

In addition, the Framework assumes no need to provide equity from prior operations to cover FY-2012 through FY-2014 operations of the Land Sales Fund. Further, the ending equity at September 30, 2011 is comprised of \$4.1 million (\$3,541,000 of reserved equity with the remaining amount unreserved). The planned use of equity as adopted in the operating budget for the next several years would have essentially resulted in budgeting into a deficit – actions would have been required to address this matter as doing so is not permitted. Given the auctions have covered all costs and have added to equity over the past several years (or thrown off enough ending equity to transfer funds into the General Fund), this matter is largely moot. The sales proceeds budgeted amount will be increased to reflect the needed coverage of operating costs – there will be no need for a planned use of equity and the amounts have been adjusted in the Summary Schedule accordingly.

Note E – Fringe Benefit Adjustment

The County included a 6% growth factor for each of the fiscal years for healthcare costs for FY-2012 and beyond. The increase, when compared to all benefits charged and based on an analysis of the closed Fringe Benefit Fund, has determined that this growth factor is now considered to be too high. When comparing the healthcare and prescription drug costs included in the operating budgets for FY-2012 through FY-2015 to a lowered amount based on actuals through FY-2011, the County has increased these combined line items by roughly

\$4,100,000 (9 months from January 1, 2012 to September 30, 2012) and \$5,466,000 each fiscal year thereafter. This will still leave adequate increases in healthcare and prescription growth over the next several years.

Note F – Personal Property Tax Elimination

During the early part of 2011, a bill was introduced that would fully eliminate personal property tax revenues with no replacement revenue. Most personal property tax revenues flow to the local units of government. In Oakland County's case, the annual revenue amount is roughly \$15.0 million for all three classes of personal property: utility, industrial and commercial property. The assertion by the bill sponsors is that by eliminating personal property taxes it removes a barrier for location of a business in Michigan and / or expansion that would provide added jobs.

Over the past several months, the discourse involving the elimination of personal property taxes has been intense. At present, there appears to be a focus on only the industrial component as the vehicle to assist in garnering new economic development and new jobs. Further, it also appears that a phase out of the tax is being supported by the Governor, with some replacement revenues. The Senate seems to oppose the replacement of revenue. The final resolution of this matter is unknown, but it is clear that some portion of the revenues may well be eliminated and not restored.

As such, the Summary Schedule has assumed that the industrial component of personal property tax revenues will be eliminated through a phase out dependent upon cutting off any new additions sometime in the future (thus, depreciation of the values over the next several years would accomplish the phase out of this revenue source). The legislation would likely move sometime in the spring 2012 and would therefore, have little or no impact on FY-2012. The Summary Schedule has assumed these conditions of lost revenue with no replacement over the period FY-2012 through FY-2015.

Given the estimated taxable value of the industrial personal property taxes as of December 31, 2011, and assuming the complete elimination of new acquisitions from being added to the tax rolls, and a five year phase out of the industrial personal property taxes, the annual decline will be \$850,000 for each of the periods from FY-2012 through FY-2015. This assumes the legislation is adopted prior to the July 1, 2012 County levy date (thus, no proration for a partial year loss would occur as the levy is deep into the County's fiscal year).

Note G – Diverted Felons

Over the past several years, the diverted felon revenue (i.e. reimbursement for felons held locally in the County jail rather than State prison) was passed late into the State's fiscal year and quite often after the Board of Commissioners took action on the County's operating budget. In FY-2011, the State passed its operating budget for FY-2012 in the summer with diverted felon

revenue included in the budget. In FY-2011, the revenue was budgeted at \$1.7 million but actually came in at \$2.1 million for a favorable variance of \$.4 million.

The State revenues and operations are being restructured and it is appearing that the longer-term view of diverted felon revenues will be that it will be included in the budgets. Years ago, this revenue was over \$4 million and has fluctuated quite a bit since then. While there is a possibility that the revenue would be eliminated, the response from the County could be that the offenders could be sent to prison rather than being held locally.

There is some exposure to including this revenue in the Summary Schedule in that it may not be received for FY-2014 and beyond, but because of the matters cited above it has now been reflected in the Framework projections. In the event that the FY-2013 revenues are reduced by the State, the County still has time to react for the remaining years. It warrants continued monitoring but at this point in time seems prudent to provide for some revenue in the FY-2014 and beyond years.

Note H – Information Technology Equipment Replacement

The Information Technology Fund cannot continue to internally fund its computer equipment replacement without adjusting its rates. Presently, there are a number of vacant positions in the Information Technology Fund. County administration is evaluating longer term structural operations that could result in some of these positions being eliminated. It is too early to tell at this writing. However, the condition of the depreciated assets and financial condition of the Fund requires that some amounts be included in the future for computer equipment replacement. The amounts included in this Framework provide a nominal contribution from the General Fund in future years when compared to the accumulated depreciation as of September 30, 2011 (\$50.6 million) and the assumption that much of this now fully depreciated equipment will eventually have to be replaced.

Note I – General Favorability / Employee Turnover

With the County's program of a hiring freeze and the restructuring of operations resulting in position deletions and the under-filling of positions, a provision to reflect anticipated annual favorability due to 'turnover' has been made in the Summary Schedule. These 'turnover' impacts, the designed delays of hiring full-time personnel, the active management by operating departments holding the line on spending and the effect of departments starting their budget tasks early has contributed to the FY-2011 ending General Fund equity above targets.

In the prior year, a \$5.0 million 'general favorability / turnover' provision was included in the Framework. It seems this project has been too low. Over the last several years, including departmental budget tasks started early in order to balance FY-2012 and beyond operations through FY-2014, the favorability has ranged from \$4.0 million in FY-2007 to \$42.6 million in FY-2010 when a concerted County-wide push was initiated to counter significant reductions in

property tax revenues, reductions in State and federal support and a general reduction in fees caused by the national and regional economy.

There are several other factors that play into the provision increasing projected “turnover” favorability. One large one is the fact that roughly one-third of County full-time personnel will be eligible for retirement between FY-2012 and FY-2015. In addition, with the recent reduction on salary rates by 4.0%, those employees still in the defined benefit programs have left in increasing numbers. Those that are replaced are replaced by employees having less costly benefits. Except for the Act 312 employees, replacement employees are brought in under the defined contribution pension plan, with a Health Savings Account (e.g. retirees’ healthcare defined contribution program). Many of the former employees also had longevity pay, a cost no longer paid (see subsequent benefits taken in the Framework for anticipated employees who likely will retire).

While the above discussion certainly bodes well for the increase in the “turnover” provision, one must note that while the County operating departments reduced the operating budget the *actual* operations often do not necessarily follow the budget reduction dollar for dollar. If not managed, unfavorable variances are more likely in these circumstances.

Looking solely to the net favorable variances for salaries and fringe benefits for the period FY-2008 through FY-2011 the cumulative favorable variances in the General Fund amounted to \$22,992,000, or on average \$5.75 million. With the anticipated *increased* retirement of employees, it is likely that the turnover benefits will continue into the next several years. When added to all other favorable variances other than compensation, it seems prudent to increase the general favorability and turnover by another amount up to \$7.5 million.

This favorability essentially offsets the need for immediate new budget tasks into the next several years. In addition to this amount, the County must also be cognizant that quarterly favorability is often used to address immediate and unknown smaller dollar operating issues that arise during the year; such amounts, while not specified in this Framework document, nevertheless occur and will be required.

Overall, the increase of the general favorability and turnover is warranted and for purposes of this Framework set a \$7.5 million. The final Framework document, which will have first quarterly results for FY-2012, will reassess this dollar amount for formal setting of budget tasks, if needed, in the near term.

Note J – Longevity Impacts - Turnover

The Human Resource and Management & Budget Departments determined that there are 290 County employees receiving longevity pay in the General Fund at an annual cost of \$1,839,000. A modest number of individuals are assumed to retire over the next four years (FY-2012 – 25 employees; 40 in each of the fiscal years 2013 through 2015), the average benefit of the

elimination of longevity paid for those employees was calculated and reflected in the attached Summary Schedule.

Note K – Infrastructure Needs

A nominal, unspecified provision for infrastructure improvements arising from delayed maintenance is provided. This matter will be revisited in more detail in connection with the final Framework report.

Note L – Motor Pool Fund Return of Working Capital

As noted previously, the Motor Pool Fund will return \$500,000 in past working capital advances provided by the General Fund while the rate structure and other operating issues were implemented and the Fund stabilized. The transfer back to the General Fund is projected to occur in the first quarter of FY-2012.

Note M – Indigent Medical Care Cost: Elimination

The County has provided \$1.0 million annually in indigent medical care to hospitals over the recent past and similar appropriations have been provided for FY-2012 through FY-2014 (and thus, the amount would be incorporated in the summary results of FY-2015). Because of the passage of the national healthcare targeted at tens of millions not presently covered or underinsured, the need to continue any funding from the County's General Fund starting in January 2014 is no longer necessary. National healthcare will cover these individuals. Therefore, three quarters of the annual cost was eliminated in FY-2014 and a full \$1.0 million in FY-2015.

Note N – General Fund Equity Target

The General Fund equity target for September 30, 2015 has been calculated at \$85 million and remains unchanged from the prior year level. The equity position measured against the expenditures anticipated for FY-2015 is 20.0% ($\$85\text{M} - \text{equity} / \$424.7\text{M} - \text{expenditures}$).

The projected equity position should be adequate to address cash flow needs for normal operations.

However, the County will still have to borrow tax anticipation notes starting circa FY-2013 arising from the changes in the property tax calendar imposed on counties several years ago by the State; such interest costs on the notes to be borrowed has been included in the adopted budgets starting in FY-2013.

PENSION PROJECTIONS - DEFINED BENEFIT PLAN

EXHIBIT A

**OAKLAND COUNTY, MICHIGAN
November 28, 2011**

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
A. Funding Value Beginning of Year	\$ 746,695,624	\$ 799,307,403	\$ 791,541,576	\$ 750,432,703	\$ 745,094,735	\$ 727,723,330	\$ 732,091,386	\$ 735,975,568	
B. Market Value End of Year	839,788,608	692,291,629	661,923,463	686,897,735	657,566,888	680,566,888	702,566,888	723,566,888	
C. Market Value Beg of Year	781,709,386	839,788,608	692,291,629	661,923,463	686,897,735	657,566,888	680,566,888	702,566,888	
D. Non-investment Net Cash Flow	(31,213,914)	(37,964,875)	(36,713,053)	(38,275,765)	(41,784,865)	(44,000,000)	(46,000,000)	(48,000,000)	
E. Investment Income:									
E1 Market Total (B-C-D)	89,293,136	(109,532,104)	6,344,887	63,250,037	12,454,018	67,000,000	68,000,000	69,000,000	
E2 Assumed Rate of Income (I)	7.5%	7.25%	7.25%	7.25%	7.25%	7.25%	7.25%	7.25%	
E3 Amount for Immediate Recognition I x (A+D/2)	54,831,650	56,573,560	56,055,916	53,018,874	52,504,667	51,164,941	51,409,125	51,618,229	
E4 Amount for Phased-In Recognition (E1-E3)	34,461,486	(166,105,664)	(49,711,029)	10,231,163	(40,050,649)	15,835,059	16,590,875	17,381,771	
F. Phased-In Recognition of Invest. Income									
F1 Current Year (E4 / 3); (E4/5 2010 & beyond)	11,487,162	(55,368,555)	(16,570,343)	2,046,233	(8,010,130)	3,167,012	3,318,175	3,476,354	
F2 First Prior Year	17,506,881	11,487,162	(55,368,555)	(22,127,310)	2,046,233	(8,010,130)	3,167,012	3,318,175	
F3 Second Prior Year	-	17,506,881	11,487,162	-	(22,127,310)	2,046,233	(8,010,130)	3,167,012	
Third Prior Year	-	-	-	-	-	(22,127,310)	2,046,233	(8,010,130)	
Fourth Prior Year	-	-	-	-	-	-	(22,127,310)	2,046,233	
F4 Total Recognized Investment Inc.	28,994,043	(26,374,512)	(60,451,736)	(20,081,077)	(28,091,207)	(2,796,886)	(1,524,943)	9,961,541	
G. Funding Value End of Year (A+D+E3+F4)	799,307,403	791,541,576	750,432,703	745,094,735	727,723,330	732,091,386	735,975,568	749,555,337	
H. Difference - Market & Funding Value	40,481,205	(99,249,947)	(88,509,240)	(58,197,000)	(70,156,442)	(51,524,498)	(33,408,680)	(25,988,449)	
I. PV of future benefit payments, less PV of employee contributions - net	697,801,950	713,289,892	717,132,705	722,435,108	732,435,108	743,435,108	755,435,108	768,435,108	
Less valuation of assets (G)	799,307,403	791,541,576	750,432,703	745,094,735	727,723,330	732,091,386	735,975,568	749,555,337	
Assets > Accrued Benefits	\$ 101,505,453	\$ 78,251,684	\$ 33,299,998	\$ 22,659,627	\$ (4,711,778)	\$ (11,343,722)	\$ (19,459,540)	\$ (18,879,771)	
PROJECTED CONTRIBUTION - Note A	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 960,260	\$ 2,311,851	\$ 3,965,854

Note A - Projected annual required contribution (ARC) is calculated based on the ratio of ARC to PV of total unfunded value of future payments based on the results of the actuarial valuation report for September 30, 2010.

Note B: Ratio: ARC to PV of UAL 0.2038

Note C: The pension contributions cited above are largely dependent on the pension system's performance two year's prior to the contribution. The FY-2011 investment performance, benefit payments and future benefit payments largely drive the need for a FY-2013 contribution. These factors in FY-2015 have not been presented because it would impact the FY-2017 pension contribution and is outside the Framework's immediate period of concern.