



March 21, 2005

The Honorable Mayor and
Members of the City Council
801 Crawford Street
Portsmouth, Virginia 23704

Dear Council Members:

I am very pleased to submit the City Manager's recommended fiscal year 2005-2006 Operating Budget and Capital Improvement Program (CIP). I am recommending an operating budget of \$448.5 million, a 5.2 percent increase over the FY05 budget, and CIP funding of \$29.8 million, of which \$10.3 million is City bond funding. These budgets have several major themes, including increased funding for education, progress on financial strategies, improving the City's economic prosperity, transforming neighborhoods and communities, investing in employees, leveraging technology to improve services, improving public safety capabilities, and strategically marketing Portsmouth.

If approved, the operating budget will provide an additional \$5 million in local support for Portsmouth Public Schools, which includes \$3.4 million in increased operating funds and \$1.6 million toward "market catch up" teacher pay raises. This increase represents a significant shift in the proportion of funds devoted to public schools in the City's budget and supports City Council's commitment to make education its highest priority. The budget also includes an additional \$3.1 million in funding for City employees, including a 3 percent general wage increase, pay range adjustments, retirement and Social Security contributions, and health insurance increases. These increases are made possible by an improved revenue picture, largely due to an improved national economy and returns from investments made by the City in the past. As noted in the media, real estate assessments have increased 13.4 percent in Portsmouth, although this percentage is considerably lower than increases in surrounding cities. Increased revenue from reassessments will be partially offset by a one-cent rollback in the real estate tax. The cutback of one cent per year is intended to fill Council's three-year goal last year when Council increased the real estate tax by three cents. In addition, other local taxes grew by 10.7 percent.

BACKGROUND

These budgets provide a detailed operating and capital “spend plan” that is directly connected to the City’s strategic planning and serves as a one-year framework for driving City Council’s long-range goals into day-in, day-out work. Thus, the task in developing these budgets is to address Council’s commendable “dreams” for the community within the context of existing programs and services and to make appropriate adjustments as priorities are clarified or modified. It is well known that the City has a considerable backlog of needs and community expectations and it is a substantial challenge to focus limited resources for effective results. All of Virginia’s cities are constrained by the Dillon Rule of state sovereignty over localities, that includes dependency on regressive taxes on property instead of more progressive taxes on income, the inability to expand or annex, and limited means for addressing aging infrastructure and population needs.

Portsmouth has the additional disadvantage of having *more than half* of our real estate off the tax rolls because of our heavy concentration of federal, state and non-profit institutions. We recognize that institutions like the Navy, the Coast Guard, Virginia Port Authority and Maryview Medical Center are economic and employment generators – primarily for state revenue – and that these institutions underpin and stabilize our economy through provision of stable jobs for some of our people.

While we have a backlog of needs and expectations and could wisely spend and invest millions more than are in these budgets, Portsmouth is fortunate to have made progress in stabilizing our financial condition, with competitive taxes and fees, reasonable debt payments and increasing revenue sources. In addition, the City Council has taken the initiative this year to develop a clear vision of where the community is going in the future, and these budgets are an effort to align our resources with that vision.

PREAMBLE

The City Council and the management team have been working very hard this year on transforming the way we do business as a City government by directly connecting our plans with actions. Several major concurrent initiatives are relevant:

City Council Vision. City Council has adopted a Vision Statement with six major Vision components, and all seven of our Council members signed this Vision Statement in a public ceremony. That signed Vision Statement has been framed and displayed in City offices all over the community. The Vision Statement is a promise of hope for citizens and their communities about the city’s future. It is a word picture of what is being envisioned. By utilizing this document and other ongoing efforts, City staff is in the process of aligning our programs and activities to achieve the Vision. These budgets represent a significant, transformative step toward achieving the Council’s Vision for the future of Portsmouth and represent a new way of doing business by being held accountable for envisioned results.

Comprehensive Plan. The City government began work on a new comprehensive plan in 2002, with significant public input achieved through public meetings, focus groups and surveys, conducted under the aegis of the Planning Commission and a Citizen 2025 Comprehensive Plan committee. This work has culminated in the committee presenting its recommended Comprehensive Plan to the Planning Commission in December 2004, and the Commission presenting the plan to the Council the first of this year. City Council had a public work session on the plan on March 7, a public hearing March 8, and is scheduled to take action on the plan next month. Coupled with the new Council Vision, the new comprehensive plan offers a more exact road map for our community. The combination of these two community-focused documents positions Portsmouth to head in new, productive directions.

City Council – School Board Cooperation. Both the City Council Vision and the Comprehensive Plan have identified education as the community’s number one priority. In support of that priority, the City Council and the School Board have already held a series of joint meetings with the goal of developing a new spirit of cooperation and launching a joint initiative that will result in a “preferred educational system” (words from City Council’s Vision Statement). The Council and School Board have signed a “Pledge of Mutual Cooperation” that says “we have the potential to ignite the fires of endless achievement for our two elected bodies in the years to come.” The two governing bodies have also endorsed a program to establish a joint financial system. These budgets are also the work of the City and School executives working closely together. The budgets propose allocations of resources that have been closely discussed by the respective staffs prior to submission to the City Council and the School Board.

High Performance Organization. While the above plans and pledges have been publicly underway, we have been working within the City government organization to better prepare ourselves for implementing the activities that carry out the goals of the City’s elected leadership. Within the Office of the City Manager we have established ourselves as an Executive Management Team (EMT) as a way of defining our jobs more broadly and connecting more with the community and City Council. We are also committed to enlarging the roles of department heads in the execution of their duties. Each of these efforts will allow us to modernize the organization, to include better utilization of technology in the delivery of services and use of information, but more importantly, in defining the fundamental job of public service at all levels as “community building.” Our key daily question is: How can we best work with the community in fulfilling the City’s Vision. To that end, we are blessed with great public employees, but we need to refocus and in some cases redirect our efforts as we face the future.

BUDGET OVERVIEW

Major themes that are incorporated in these budgets include:

- Increased funding for education
- Progress on financial strategies

- Improving the City’s economic prosperity
- Transforming neighborhoods and communities
- Investing in our employees
- Leveraging technology to improve services
- Improving public safety capabilities
- Strategically marketing Portsmouth

Many of these themes support several of Council’s six Vision components, which are:

- Bold New Directions
- Lifelong Learning Community
- Neighborhood and Community Transformation
- Robust and Prospering Economy
- World Class Maritime Center
- Pride of Past, Promise of Future

For example, supporting the Schools budget is, in and of itself, a Bold New Direction that helps us achieve a Lifelong Learning Community while contributing to Neighborhood and Community Transformation and a Robust and Prospering Economy, and supporting our Pride of Past, Promise of the Future. It is within the realm of reality that achievement of a “preferred educational system” is a significant step in supporting a World Class Maritime Center.

In the same vein, our budget themes of investing in our employees and leveraging technology to improve services also support most if not all of the Council Vision Statements. Enhancing our workforce and making better use of technology are both focused on improved customer services, which is at the very heart of the mission of local government and supports all of our efforts to move forward.

Following is a discussion of the major themes of this budget presentation.

Increased funding for education

This budget fully funds the School Superintendent’s baseline budget recommendation (as submitted on March 4, 2005), providing an increase of \$3.4 million in operating funds, which includes a salary increase for teachers of 5.5 to 6 percent. In addition to teacher salary increases, the \$3.4 million requested by the Superintendent from the City includes non-teacher salary increases, technology upgrades, middle-school enhancement programs, nurses’ salaries, and retirement and health insurance funding.

The recommended budget also includes an *additional* \$1.6 million to support the first year of the School Board’s plan to bring school teacher salaries to parity within the region over three years. The FY06 “installment” will provide an additional 3 percent

salary increase for teachers. The City also intends to continue to support the School Board's "catch up" plan, as resources will allow in the coming years.

The total increase in City funding for the Schools is \$5 million, from \$31 million in FY05 to \$36 million in FY06— an increase of 16 percent. The \$5 million increase will provide *total teacher salary increases of 8.5 to 9 percent*. The \$5 million increase is more than double the \$2.2 million increase in City funding for the Schools in FY05.

The significance of the City's funding effort can be measured in other ways as well:

- The percent of total local tax revenue (exclusive of utility taxes) in the City's budget has grown from 28.5 to 30 percent.
- The percent of the City's *total new money* dedicated to Schools is 39 percent.

The CIP includes funding of \$2.1 million for the new Park View Elementary School, with construction scheduled to begin in the FY06 fiscal year. The CIP also includes \$500,000 for renovations to Highland-Biltmore Elementary School, \$500,000 for Churchland High School air quality improvements, and \$3.6 million for major renovations at various schools, including roof, boiler and HVAC improvements.

Progress on financial strategies

The City's national financial advisers, Public Finance Management (PFM), in 2003 recommended a number of significant financial management policies in order to restructure and improve the City's financial condition. These policies, and their results, are closely monitored by bond rating agencies (Moody's, Standard & Poor, and Fitch). Each year Portsmouth's fiscal health is reviewed and compared in detail with other local governments for purposes of determining the City's bond rating. We are currently rated AA- (double A minus). While our rating is currently "investment grade," it is not as advantageous as some of our neighbors. In addition, the City has been on a "bond rating watch" the last two years for a possible downgrade of its rating. Our commitment to and performance within strict financial policies has allowed us to navigate successfully through these troubled waters.

The first of these policies is to achieve an unreserved and undesignated General Fund balance target of 12.5 percent of General Fund revenues in order to maintain strong cash reserves for the City and to ultimately eliminate the need for short-term borrowing to meet financial obligations. Effective June 30, 2004, the City had reached 10.4 percent.

Another financial standard calls for the City to develop a Capital Improvement Program on a prioritized basis, and to use CIP funding to fulfill these established priorities. The City has recently completed a five-year financial forecast to serve as the basis for financing capital projects.

Other CIP principles guiding the City are: maintain debt affordability; give priority to public safety and education projects; address ongoing maintenance and replacement needs; give priority to projects supporting private development; and schedule funding in the year to be spent. The City is using these principles to guide its capital budgeting.

One of the largest concerns of PFM, the bond rating agencies and the City's financial staff involves the two Portsmouth retirement systems which were "closed out" several years ago. These two systems have about \$101 million in unfunded liabilities. On the one hand, the benefits associated with former City employees under these systems represent "promises" for their retirements, which are underway, while these systems' liabilities are ongoing and continuing for the City in a "catch up" mode. The recommendations contained in this budget continue to fund these systems on a sound actuarial basis.

We are continuing to implement modest phased rate increases in our water, sewer and stormwater systems. Planned rate increases included in the FY06 budget are an increase from \$3.00 per 1,000 gallons to \$3.15 per 1,000 gallons in residential water rates, from \$2.27 per 1,000 gallons to \$2.42 per 1,000 gallons in residential sewer rates, and from \$4.00 per ERU to \$4.50 per ERU in stormwater rates. These rate increases enable us to continue to upgrade the infrastructure supporting those utilities. We are also redirecting public utility funds to neighborhood infrastructure needs in the FY06 budget by reducing the amount of those funds directed to the General Fund.

We are also continuing to make progress on reducing funding from the General Fund to support other funds such as Information Technology, Golf, Waste Management, Risk Management and Insurance Fund, Health Insurance Fund and others. By reducing the General Fund support of those other funds, we strengthen the General Fund and increase our ability to maintain a sound fund balance, while continuing to keep the other funds whole.

Compliance with our CIP debt limitation policy is a critical goal. We have constrained our capital requests and are recommending a FY06 CIP of \$29.8 million, of which \$10.3 million is City bond funding in keeping with that policy. Though we have been unable to fund all recommended requests, maintaining our debt limitation policy enables us to keep our capital spending in line with debt affordability.

The budget includes a recommended one-cent reduction in the real estate tax rate, from \$1.45 per \$100 of assessed value to \$1.44. This represents a one-cent "rollback" in keeping with City Council's commitment last year when it increased the real estate tax rate from \$1.42 to \$1.45. It is City Council's goal to continue a one-cent rollback each year for the next three budget years.

City Council is also concerned that real estate be fairly and equitably assessed throughout the City, and that real estate be assessed as close to market value of property as is feasible. In keeping with this concern, it is the intent of the Council to conduct a real estate assessment study in the coming fiscal year.

Improving the City's economic prosperity

The proposed operating budget includes partial funding to support the beginning of multi-year phase-in implementation of the Comprehensive Plan. Specifically, we are including funds for the Downtown Master Plan, Waterfront Hot Spots Development Study, Downtown Parking Strategy and Downtown Rezoning Plan.

In addition, these budgets support some economic development projects that are having a major impact on the City. The Pinners Point connector is a vital transportation link that will allow the ongoing enhancement of the City as a world-class maritime center. Construction by APM Terminals of Virginia Inc. (also known as the "Maersk project") of a major new cargo terminal on their 557-acre site will further enhance the City's status as a world-class maritime center. The completion of the Pinners Point connector is an essential transportation element to the terminal's operation. City funding for neighborhood improvements related to the terminal's development will be included in the FY07 budget.

As a continuing means of supporting the strengthening of education within the city, the new Portsmouth campus of Tidewater Community College will be constructed as an element of the Victory Crossing Business Park. The City will support the campus development by funding the necessary infrastructure to support the buildings that will make up the campus. Partial funding for the infrastructure is included in the FY06 CIP. To support the business park and college campus, the City, in collaboration with VDOT, will also bring about the improvement of the section of Victory Boulevard between Cavalier Boulevard and Greenwood Drive. That project will be initiated in FY06.

As a means to bring about the Council's Vision of restoring retail to the Midtown corridor, the former Mid-City Shopping Center has been acquired and is in the process of demolition. In addition, certain elements of infrastructure will be funded to bring this initiative to fruition.

Transforming neighborhoods and communities

Through the City Council's Vision, I believe we have a unique opportunity to rethink our neighborhoods and develop additional solutions that will make them more vibrant, exciting and desirable communities in which to live well into the 21st century. If we want to develop neighborhoods that will be great places to live now and into the next century, we need to understand, and to be able to describe and measure the basic elements that define good neighborhoods - homes in good condition, adequate parking, good transportation, quality shopping, nearby playgrounds and libraries, and safe streets. I am recommending several important project initiatives within the Capital Improvement Program that will directly impact and improve the quality of live within neighborhoods across our City.

The first of these has to do with the Churchland Library. The Churchland community has outgrown the capacity of the existing public library. Although we have explored options

with neighboring cities for regional partnering, such opportunities are not available at this time. I am proposing \$100,000 in the FY06 budget toward the initial design and planning phase for the new Churchland Library.

I am proposing funding of \$100,000 for the demolition of 23 vacant dwellings within neighborhoods across the City, as part of our continuing efforts to take out condemned and unsafe structures. In addition, \$75,000 is included for weeds and debris removal from private property. The Department of Community Relations and Leisure Services will manage this initiative.

As part of the continuing work in the Victory Crossing area, the FY05 budget includes \$100,000 designated for landscaping in the area of the westbound off-ramp from I-264 at Victory Boulevard and for the median of Victory Boulevard in the area of the Victory Crossing Shopping Center. The FY06 budget includes \$1,725,000 to continue the effort of making improvements to Victory Boulevard between Cavalier Boulevard and Greenwood Drive. Landscaping will be an essential part of this work and will serve to assure that the improvement and beautification of the area continues.

The budget includes \$550,000 for the installation of storm drainage piping and closure of the median drainage ditch on Cavalier Boulevard from Greenwood Drive to Victory Boulevard. This project will also include upgrades to the water and sewer lines in the same area, to be funded through Public Utilities. There is \$417,600 in the FY05 budget for drainage issues in this area.

The Neighborhood Quality Action Plan (NQAP) includes a component on improving the appearance of gateway entrances to the City through more positive visual elements such as landscaping and improved signage. The budget includes \$200,000 to be appropriated for this neighborhood transformation initiative. The focus in the FY06 budget will be on North Landing, High Street Landing, High Street corridor and Portsmouth Boulevard at Hodges Ferry Bridge.

Investing in our employees

Employees are any agency's most important asset. Portsmouth is blessed to have competent employees who have established a long-time work culture of meeting and surpassing the expectations of our citizens. The public's work is often performed under difficult conditions, including constrained financial resources. This budget begins to better address the needs of our employees. These are early steps on a long journey to modernize the organization.

This budget includes an additional \$3.1 million for City employees, in general wage increases, pay range adjustments, retirement and Social Security contributions, and health insurance increases.

As part of proposed pay range adjustments, we are making market adjustments for sworn police personnel, which is described in more detail in the section on public safety.

In this budget we have included a 3 percent general wage increase effective July 1, 2005, on the current salaries of all City employees. The general wage increase will facilitate the movement of employees within their respective pay ranges. The budget also includes a 1.5 percent cost of living adjustment for all retirees in the City of Portsmouth retirement systems. To increase the competitiveness of our pay system within our defined market of Norfolk, Chesapeake, Virginia Beach, Suffolk, Newport News and Hampton, we have made a structure adjustment of 5.25 percent to our pay ranges to enhance employee growth and retention. The movement at the end of the ranges will provide the opportunity for pay increases to employees whose salaries have approached the end of the range. In addition, City positions have been evaluated in comparison to similar positions within our defined market. From those evaluations, we have identified City positions that required immediate adjustments, which resulted in reclassification of those positions. Overall, we are recommending City Council set 90 percent of market value as our ongoing compensation goal. This will allow the City to have a specific benchmark for continuing measurement and community discussion.

For FY06, the City is increasing its employee health insurance funding by 10 percent, effective January 1, 2006. Overall, this budget recommends more than \$3 million be added to City employee wages and benefits.

There is still much to do for City employees in the future.

Our investment will foster a learning organization, where continuous learning is not only encouraged but also supported through the Tuition Assistance Program and training opportunities funded in individual departments. The City continues to encourage employees to take advantage of opportunities to improve their knowledge and skills, resulting in job enrichment and improved customer service.

During the coming fiscal year, the Department of Human Resource Management will revise, enhance and reintroduce the Employee Incentive Program, which provides cash awards for cost-saving suggestions. The program will encourage cost-saving responsibility, creativity and innovation, and continue to promote a positive image of the City. In addition, the City recognizes our extraordinary employees through the Employee of the Month Program and Employee of the Year Program, as well as our annual Service Award Recognition Program. For FY06, the City will also introduce a new team award program that supports the City's value of teamwork.

Leveraging technology to improve services

The budget includes a number of projects which will advance Portsmouth in the area of technology, resulting in improved customer services. The first of these is the relocation and upgrading of our Emergency Communications Center/E911 and the Emergency Operations Center (EOC). This is being funded over a five-year period using lease purchase at a total cost of \$1.3 million, with \$320,000 in lease payments included in the FY06 operating budget. The current fiscal year is the first year of that five-year process. The upgrade will include the replacement of obsolete call taking and radio dispatching

equipment with modern, state-of-the-art technology. The plan for FY06 is to have the new ECC and EOC completely staged and ready for operations.

The CIP includes \$2 million toward funding of the City and School collaborative systems project to replace internal finance software with a modern comprehensive financial and human resource management system. This project already has received a contribution of \$936,486 from a prior year's fund balance of the School system. The new system will provide business process improvements within financial operations and automate current manual record keeping and reporting. A new comprehensive financial system is needed to integrate and improve workflow, re-engineer processes, reduce paper record keeping and provide better access to financial data within City departments and the Schools. The purchase and implementation of a financial system to meet the needs and requirements of both organizations is most cost effectively performed as a partnership between the City and the Schools.

The budget includes funding for a new mobile computing system for code enforcement that has a total lease purchase cost of \$221,250, with \$82,600 in lease payments included in the FY06 operating budget. This technology will provide city code enforcement inspectors real-time access to the code enforcement database from the field. Real-time wireless access to the code enforcement database allows inspectors to view a history of property complaints and enter code enforcement cases directly from the field, allowing them to spend more time on the street completing field work and less time in the office entering case information.

The State Social Services system currently requires entry of redundant data on separate computer platforms. The EZ-Filer system is a single-computer interface that reduces the amount of time that local agencies spend in accessing and updating client and case information. Casework load studies have shown a 50 percent reduction in the amount of time it takes for an eligibility worker to complete a search of State systems. The total system cost is \$533,750, which is included in the Social Services Department budget, and that makes this system eligible for State reimbursements.

The budget includes a technology replacement program that includes the replacement of aging computer and radio equipment.

Improving public safety capabilities

In order to adjust our pay plan to bring sworn police officers more in line with our market, the following changes in the starting pay for police personnel will be included in our FY06 pay plan: police officer, from \$29,844 to \$31,411; sergeant, from \$39,994 to \$46,409; lieutenant, from \$44,094 to \$51,166; and captain, from \$48,613 to \$56,410. These adjustments will make us more competitive for hiring in the region.

The operating and capital budgets include a number of activities to improve public safety capabilities. We are anticipating the arrival of our 47-foot fireboat later this spring to provide additional fire suppression and rescue services for the Portsmouth waterfront as

well as for other cities in the Hampton Roads region. We are looking forward to adding this enhanced public safety service to our region as we continue to build our capabilities.

As a result of lead detection in the City's police firing range, the City will temporarily use the firing range in Moyock, N.C., to meet its required firearm certification for public safety employees until a permanent solution has been determined. Additional overtime funding has been included to support this activity.

The budget includes lease purchase funding totaling \$2 million, with \$480,000 in lease payments included in the FY06 operating budget, for the continuing replacement and upgrading of public safety and other vehicles. It is necessary to continue our vehicle replacement program to ensure that public safety and other employees are provided the rolling equipment that is required in the performance of their duties.

The FY06 capital budget includes \$1.7 million in funding toward the major renovation and expansion of the Portsmouth courts facilities, which is estimated to have a total cost of more than \$20 million. In addition to planned improvements, this project will include an additional courtroom for the Circuit Court in anticipation of a new judgeship. The court renovation and expansion project has been under study for some time, and we plan to continue work on the Civic Center in FY06.

The capital budget also includes funding for public safety facilities improvements, including the Effingham Fire Station, Truxtun Fire Station, and Police Headquarters.

Strategically marketing Portsmouth

The City's marketing team has been working on a number of new initiatives, with the goal of creating an integrated marketing approach to promote Portsmouth's marketable assets. The Virginia Sports Hall of Fame has joined our City team in anticipation of the grand opening of that facility this spring. To date, the marketing team has developed a vision, mission statement and marketing goals. Work is now underway to complete an overall marketing plan for implementation in FY06.

The plan includes a number of cross-marketing strategies, including a \$50,000 promotion called "Springtime in Portsmouth" to highlight the many events and activities taking place here in the spring, building on the success of the Holidays in the City campaign last winter. The team plans to continue these cross-marketing efforts to link and integrate all of the "products" that Portsmouth has to offer.

The FY06 budget includes pre-approved support for the Virginia Sports Hall of Fame, as well as operating funding for the Portsmouth Museums and \$300,000 (\$250,000 in the CIP and \$50,000 in the operating budget) of additional support for continuing development of the Children's Museum of Virginia, matching \$300,000 appropriated for the Children's Museum by the Virginia General Assembly. The budget also includes support for Portside, a high priority of the City Council, the Path of History, and events and festivals such as the Umoja Festival, Cock Island Race, Seawall Festival, Gosport

and Seawall art shows, Holidays in the City, Winter Wonderland, Olde Towne Holiday Music Festival, TodiMusicFest and the Virginia Arts Festival. This commitment to arts and cultural activities demonstrates the City's continuing support of such activities as a vital component of the quality of life of our community.

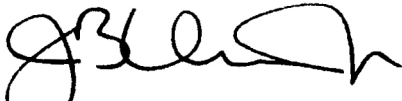
SUMMARY

The FY06 budget has been prepared within the larger context of City Council's ongoing, systematic review of basic priorities and the administration's commitment to modernize the organization.

Recently, City Council has written and published its Vision Statement and a new Comprehensive Plan has been proposed for final adoption. Meanwhile, the administration has been sorting and reviewing City operations with the goal to establish stronger managed environments. Thus, while these budget proposals offer several major adjustments toward new beginnings, the overall efforts should be considered as "works in progress."

This budget provides a detailed operating and capital "spending plan" that is directly connected to the City's strategic planning and serves as a one-year framework for achieving City Council's long-range goals.

Sincerely,

A handwritten signature in black ink, appearing to read "James B. Oliver, Jr.", written in a cursive style.

James B. Oliver, Jr.
City Manager