

Memorandum



CITY OF DALLAS
(Report No. A17-011)

DATE: September 15, 2017

TO: Honorable Mayor and Members of the City Council

SUBJECT: Audit of the Revenue Estimates Included in the Fiscal Year 2017-18 Proposed Annual Budget for the City of Dallas¹

In total, the revenue estimates included in the Fiscal Year (FY) 2017-18 Proposed Annual Budget appear reasonable (see Table III in Attachment I). The City of Dallas (City) improved documentation of revenue estimate methodologies and supporting calculations to ensure reliable revenue estimates are included in the City Manager's FY 2017-18 Proposed Annual Budget. Both the Department of Aviation (AVI) and the Department of Convention and Event Services (CES) corrected the issues noted in the prior year audit. Specifically:

- The AVI updated the FY 2017-18 revenue estimate methodology (methodology) for Rental on Airport revenues. The AVI also provided accurate and complete documentation, including supporting calculations for the Rental on Airport and Concession revenues methodologies.

- The CES improved methodology documentation and supporting calculations

Overview

- The FY 2017-18 Proposed Annual Budget of approximately \$3.0 billion is \$106.5 million, or 4.7 percent, higher than the FY 2016-17 Estimated Actual Revenues for Major Revenue Sources (see Tables III and IV in Attachment I)
- The FY 2016-17 Adopted Annual Budget for Major Revenue Sources of approximately \$2.3 billion is \$4.8 million, or 0.2 percent, below the FY 2016-17 Estimated Actual Revenues for Major Revenue sources (see Table V in Attachment I)

Source: City of Dallas

¹ The objective of the audit was to determine whether the City has effective processes to ensure reliable revenue estimates are included in the City Manager's FY 2017-18 Proposed Annual Budget. We also reviewed certain related transactions and records before and after this period. Council Resolution 904027 directs the City Auditor to review and verify the reasonableness of the revenue estimates included in the City Manager's proposed budget. This performance audit was conducted under the authority of the City Charter, Chapter IX, Section 3 and in accordance with the FY 2017 Audit Plan approved by the City Council. This performance audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. We interviewed department personnel, reviewed revenue estimate methodologies and material assumptions for reasonableness, verified mathematical accuracy, traced amounts to the appropriate FY budget documents, and performed various analyses.

Additional Observations

Other matters came to our attention concerning the revenue estimates for major enterprise and general fund operations that deserve mention, including:

Department of Aviation

The AVI's FY 2017-18 Proposed Budget includes a \$20 million, or 18.7 percent, increase from the \$107 million FY 2016-17 Adopted Budget. The AVI uses a cost recovery methodology to estimate budgeted revenues whereby incurred costs are reimbursed by the airlines using Dallas Love Field Airport. According to AVI, revenue increases primarily result from the reimbursement of the following projected costs:

- \$9.7 million for the Rental on Airport revenue
- \$5.4 million of the \$8.8 million for the Checked Baggage Resolution Area project. The total cost will be amortized over 18 months.
- \$2.4 million Debt Service payment increase for the Love Field Modernization Project

Department of Dallas Water Utilities

The Department of Dallas Water Utilities' (DWU) most recent five years continued a long-standing trend of unfavorable variances between budget and actual revenues. The total unfavorable variance for this five-year period is approximately \$127.7 million, or 4.2 percent, of operating revenues.

According to DWU:

- Seasonal fluctuations in rainfall and the effects of water conservation initiatives make developing more accurate revenue estimates challenging. To address these challenges, DWU has over time: (1) increased retail and wholesale rates charged to customers to more accurately reflect DWU's actual costs; and, (2) adjusted projected water sales when preparing the revenue estimate to more accurately reflect the results of DWU's water conservation initiatives (see Tables I and II on the following page).

Table I

**Summary of Wholesale and Retail Rate Increases
 FY 2012-13 to FY 2016-17**

Fiscal Year	2012-13	2013-14	2014-15	2015-16	2016-17
Rates – Wholesale (Percent)	2.7	2.8	2.2	14.2	6.7
Rates – Retail (Percent)	5.1	4.5	3.5	5.3	2.6

Table II

**Summary of Increase / (Decrease) in Projected Water and Wastewater Sales
 for FY 2012-13 to FY 2016-17**

Fiscal Year	2012-13	2013-14	2014-15	2015-16	2016-17
Water Sales – Wholesale (Billion Gallons)	0.6	(0.3)	(0.7)	(1.0)	(1.5)
Water Sales – Retail (Billion Gallons)	(3.0)	(0.0)	(1.0)	(1.0)	(1.0)
Wastewater Sales – Retail (Billion Gallons)	(2.0)	(1.7)	(0.7)	0.3	(0.8)

- When actual revenues fall short of budgeted revenues, DWU responds by reducing expenses where possible and cash transfers for planned capital construction projects (projects). Reductions of cash transfers may result in some project deferrals and increased costs using additional debt financing for planned capital construction.

- The amounts budgeted for projects' transfers were made for the last five years except for FY 2013-14 when more than the budgeted amount was transferred
- Unfavorable variances for FY 2016-17 would not affect projects

Department of Sanitation

For the past three years, the Department of Sanitation (SAN) continued to experience significant favorable variances between budget and actual revenues. For example, for FY 2016-17, there was a 9.9 percent favorable variance between the \$95.9 million FY 2016-17 Adopted Budget and the \$105.5 million FY 2016-17 Estimated Actual Revenues. According to SAN, the increase was mainly due to unanticipated weather events that increased McCommas Landfill (McCommas) usage by non-contracted cash customers (customers) from surrounding cities.

In FY 2016-17, SAN increased the gate rate from \$21.50 to \$25 per ton; however, many customers continued to use McCommas because of the competitive rates and extended operating hours. As a result, SAN increased the FY 2017-18 Proposed Budget by \$6.3 million, or 6.6 percent, from the \$95.9 million FY 2016-17 Adopted Budget.

Department of Trinity Watershed Management – Storm Water Fees

The Department of Trinity Watershed Management (TWM) increased the FY 2017-18 Proposed Budget for Storm Water Fees by \$5 million, or 9.9 percent, from the \$50.9 million FY 2016-17 Adopted Budget. According to TWM, the budget increase is due to a proposed 9.8 percent Storm Water fee increase.

Office of Financial Services – Ad Valorem Taxes

The Office of Financial Services (OFS) increased the FY 2017-18 Proposed Budget for Ad Valorem Taxes by \$61.8 million, or 7.3 percent, from the \$852.7 million FY 2016-17 Adopted Budget to the \$914.5 million FY 2017-18 Proposed Budget. According to OFS, the certified taxable property value in Dallas increased by 7.2 percent from \$110.4 billion in 2016 to \$118.3 billion in 2017.

Concluding Comments

The Office of the City Auditor (Office) reviewed approximately \$2.3 billion of the \$3.0 billion in proposed revenue estimates for the General Fund, Enterprise Funds, and Debt Service Fund, or 78 percent, of the revenue estimates included in the FY 2017-18 Proposed Annual Budget (see Table III in Attachment I).

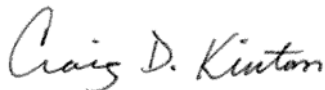
Our review did not include the remaining \$652.8 million in revenue estimates which are mainly derived from department reimbursements and City, employee, and retiree contributions for retirement and health benefits. Five-year budget-to-actual comparisons and the FY 2017-18 Proposed Annual Budget amounts for the major revenue sources are shown in Attachment II (see Charts I through VIII).

City management is responsible for preparing reasonable revenue estimates for inclusion in the FY 2017-18 Proposed Annual Budget. In preparing these revenue estimates, City management develops revenue estimate methodologies, such as regression analyses and/or historical trends, and documents the significant assumptions used to support those methodologies. This information is reviewed by the Office for reasonableness; however, neither City management nor the Office guarantees the achievement of the FY 2017-18 revenue estimates.

We would like to acknowledge City management's cooperation in providing the information needed to complete this audit.

If you have any questions or need additional information, please contact me at 214-670-3222 or Carol Smith, First Assistant City Auditor, at 214-670-4517.

Sincerely,



Craig D. Kinton
City Auditor

Attachments

C: T.C. Broadnax, City Manager
M. Elizabeth Reich, Chief Financial Officer
Majed Al-Ghafry, Assistant City Manager
Jon Fortune, Assistant City Manager
Joey Zapata, Assistant City Manager
Jo M. (Jody) Puckett, P.E., Interim Assistant City Manager
Mark Duebner, Director – AVI
Kelly High, Director – SAN
Jack Ireland, Director – OFS
Ron King, Director – CES
Terry Lowery, Director – DWU
Sarah Standifer, Director –TWM
Janette Weedon, Assistant Director – OFS
Nick Fehrenbach, Manager (Utility Management) – OFS

ATTACHMENT I

Table III

Fiscal Year 2017-18 Proposed Budget Revenue Sources Included in the Office of the City Auditor’s Assessment

Chart	Revenue Sources	Fiscal Year 2017-18 Proposed Revenues
General Fund		
I	Ad Valorem Taxes	\$ 654,493,929
II	Sales Tax	303,349,086
III	Franchise Fees	109,290,898
Enterprise Funds		
IV	Water Utilities	667,471,388
V	Sanitation Services	102,279,097
VI	Aviation - Concessions and Rental on Airport ¹	99,152,520
VII	Convention and Event Services – Hotel Occupancy Tax	59,933,282
VIII	Storm Water Fees	55,987,895
Debt Service		
	Ad Valorem Taxes	260,036,329
Total Revenue Estimates Assessed		\$ 2,311,994,424
Revenue Estimates Not Included		652,787,537
Total FY 2017-18 Proposed Budget		\$ 2,964,781,961

¹ Amounts for Aviation – Concessions and Rental on Airport were provided by City of Dallas (City) management. The \$99.2 million amount is not individually presented in the Fiscal Year (FY) 2017-18 Proposed Annual Budget.

Source: FY 2017-18 Proposed Annual Budget (Unaudited)

Audit of the Revenue Estimates Included in the Fiscal Year 2017-18 Proposed Annual Budget for the City of Dallas

Table IV

Fiscal Year 2016-17 Estimated Actual Revenues Compared to Fiscal Year 2017-18 Proposed Revenues for Major Revenue Sources

Revenue Sources	Fiscal Year 2016-17 Estimated Actual Revenues ¹	Fiscal Year 2017-18 Proposed Revenues	\$ Variance	% Variance
General Fund				
Ad Valorem Taxes	\$ 611,811,125	\$ 654,493,929	\$ 42,682,804	7.0
Sales Tax	294,451,663	303,349,086	8,897,423	3.0
Franchise Fees	114,666,826	109,290,898	(5,375,928)	(4.7)
Enterprise Funds				
Water Utilities	648,427,649	667,471,388	19,043,739	2.9
Sanitation Services	105,452,716	102,279,097	(3,173,619)	(3.0)
Aviation	105,312,695	127,028,405	21,715,710	20.6
Convention and Event Services	97,125,083	97,787,266	662,183	0.7
Storm Water Fees	50,936,837	55,987,895	5,051,058	9.9
Debt Service Fund				
Ad Valorem Taxes	243,021,373	260,036,329	17,014,956	7.0
Totals	\$ 2,271,205,967	\$ 2,377,724,293	\$ 106,518,326	4.7

¹ FY 2016-17 Estimated Actual Revenues are based on information provided by City management.

Source: FY 2017-18 Proposed Annual Budget (Unaudited)

Audit of the Revenue Estimates Included in the Fiscal Year 2017-18 Proposed Annual Budget for the City of Dallas

Table V

Fiscal Year 2016-17 Adopted Budget Revenues Compared to Estimated Actual Revenues for Major Revenue Sources

Revenue Source	Adopted Budget	Estimated Actual Revenues ¹	\$ Variance	% Variance
General Fund				
Ad Valorem Taxes	\$ 610,219,359	\$ 611,811,125	\$ 1,591,766	0.26
Sales Tax	292,188,504	294,451,663	2,263,159	0.8
Franchise Fees	113,774,789	114,666,826	892,037	0.8
Enterprise Funds				
Water Utilities	657,464,737	648,427,649	(9,037,088)	(1.4)
Sanitation Services	95,946,054	105,452,716	9,506,662	9.9
Aviation	107,026,764	105,312,695	(1,714,069)	(1.6)
Convention and Event Services	96,403,076	97,125,083	722,007	0.7
Storm Water Fees	50,936,837	50,936,837	-	0.0
Debt Service Fund				
Ad Valorem Taxes	242,487,406	243,021,373	533,967	0.2
Totals	\$ 2,266,447,526	\$ 2,271,205,967	\$ 4,758,441	0.2

¹ FY 2016-17 Estimated Actual Revenues are based on information provided by City management.
Source: FY 2017-18 Proposed Annual Budget (Unaudited)

ATTACHMENT II

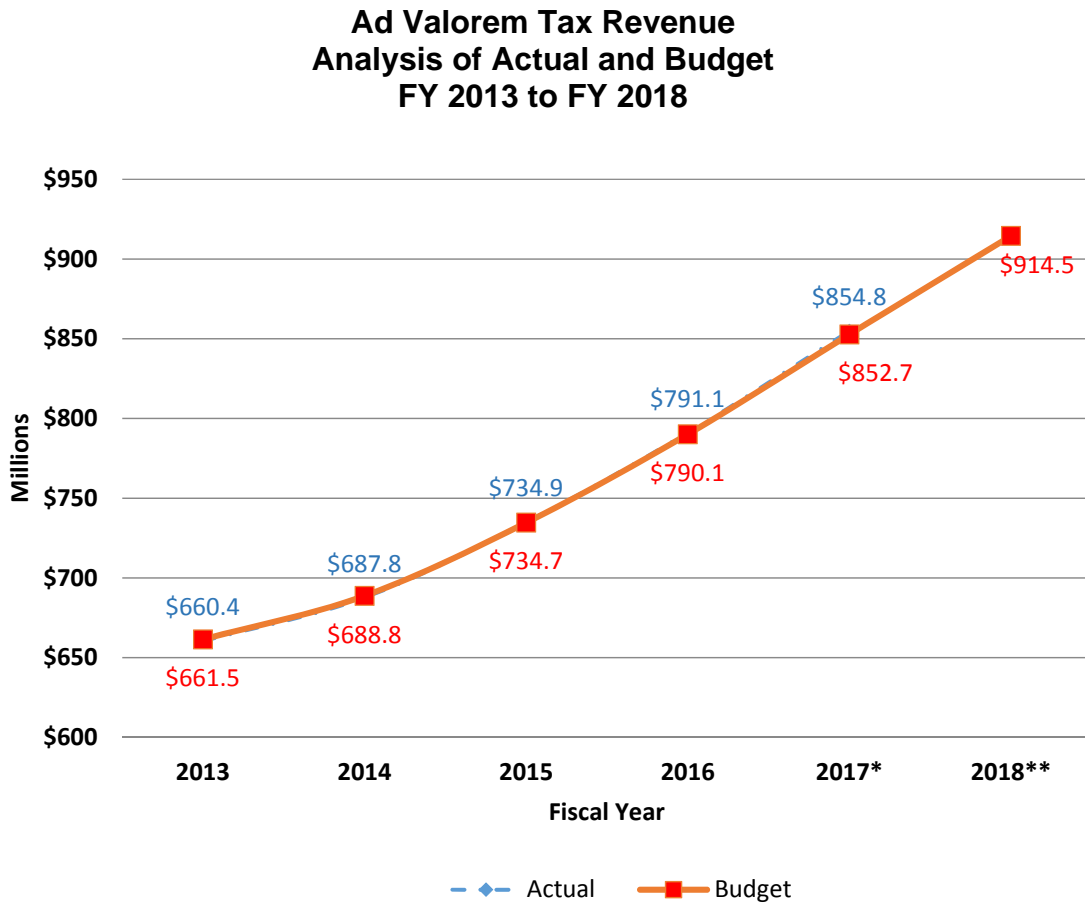
Charts I to VIII shown on the following pages are based upon analyses of Fiscal Year (FY) 2013 through FY 2018 actual and budget revenues and current year estimates included in the FY 2017-18 Proposed Annual Budget presented as of August 9, 2017. Descriptions for the revenue sources were provided by management or taken from the Office of Financial Services' FY 2017-18 Proposed Budget Appendices, *Major Revenue Sources*.

The Charts provide comparisons of the Adopted FY 2013 to FY 2016 budgets versus actual revenues collected for the same period. In addition, the Charts show the FY 2017 Adopted Budget vs. Estimated Actual Revenues and the FY 2018 Proposed Budget.

Ad Valorem Tax Revenue

Ad Valorem (Property) Taxes are the largest revenue source for the General Fund and Debt Service Fund. Assessed property values are established by the Central Appraisal Districts in the four counties (Dallas, Collin, Denton, and Rockwall) in which the City of Dallas (City) is located and are certified by the individual Appraisal Districts (Appraisal Review Boards).

Chart I



* FY 2017 revenues, including estimates for the remaining months, were provided by City management.

** FY 2018 is proposed; therefore, actual is not available.

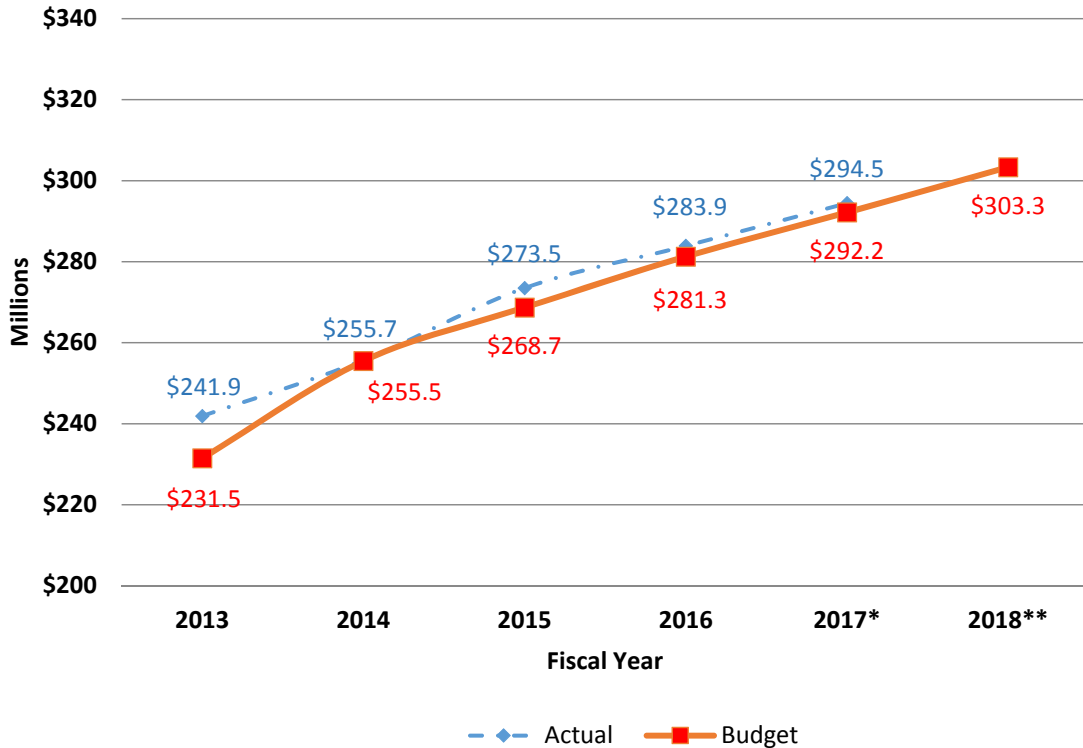
Source: City of Dallas Adopted Annual Budgets and FY 2017-18 Proposed Annual Budget (Unaudited)

Sales Tax Revenue

Sales Tax is the second largest revenue source for the General Fund. The sales tax rate in the City is 8.25 percent of taxable goods or services sold within the City limits. The sales tax is collected at the point of sale and forwarded to the Texas State Comptroller’s Office on a monthly or quarterly basis. Of the 8.25 percent collected, the State retains 6.25 percent and distributes one percent to the City and one percent to the Dallas Area Rapid Transit transportation authority.

Chart II

**Sales Tax Revenue
Analysis of Actual and Budget
FY 2013 to FY 2018**



* FY 2017 revenues, including estimates for the remaining months, were provided by City management.

** FY 2018 is proposed; therefore, actual is not available.

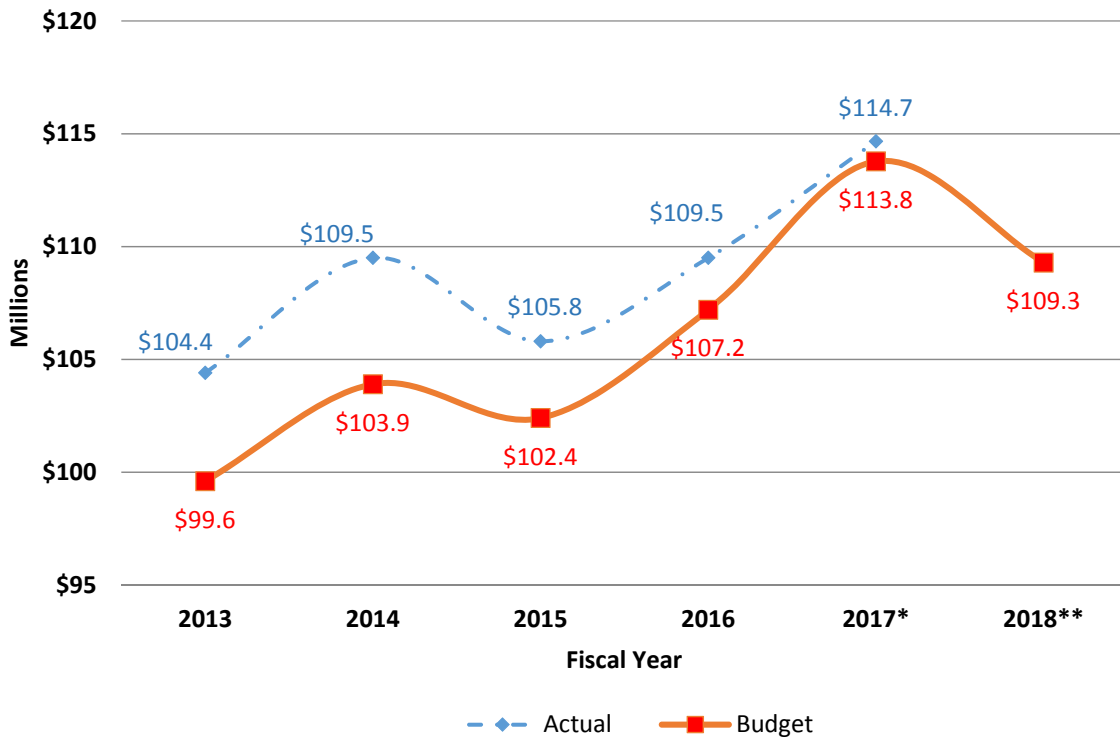
Source: City of Dallas Adopted Annual Budgets and FY 2017-18 Proposed Annual Budget (Unaudited)

Franchise Fees Revenue

The City maintains non-exclusive franchise agreements with utilities and other service providers that use the City’s rights-of-way to provide services to the public. These franchise agreements provide for compensation to the City in the form of franchise fees. These fees are in lieu of all other fees and charges related to the use of the rights-of-way.

Chart III

**Franchise Fees Revenue
Analysis of Actual and Budget
FY 2013 to FY 2018**



* FY 2017 revenues, including estimates for the remaining months, were provided by management.

** FY 2018 is proposed, therefore actual is not available. FY 2017 Estimated Actual Revenue includes the majority of a one-time \$4.1 million settlement from a utility service provider.

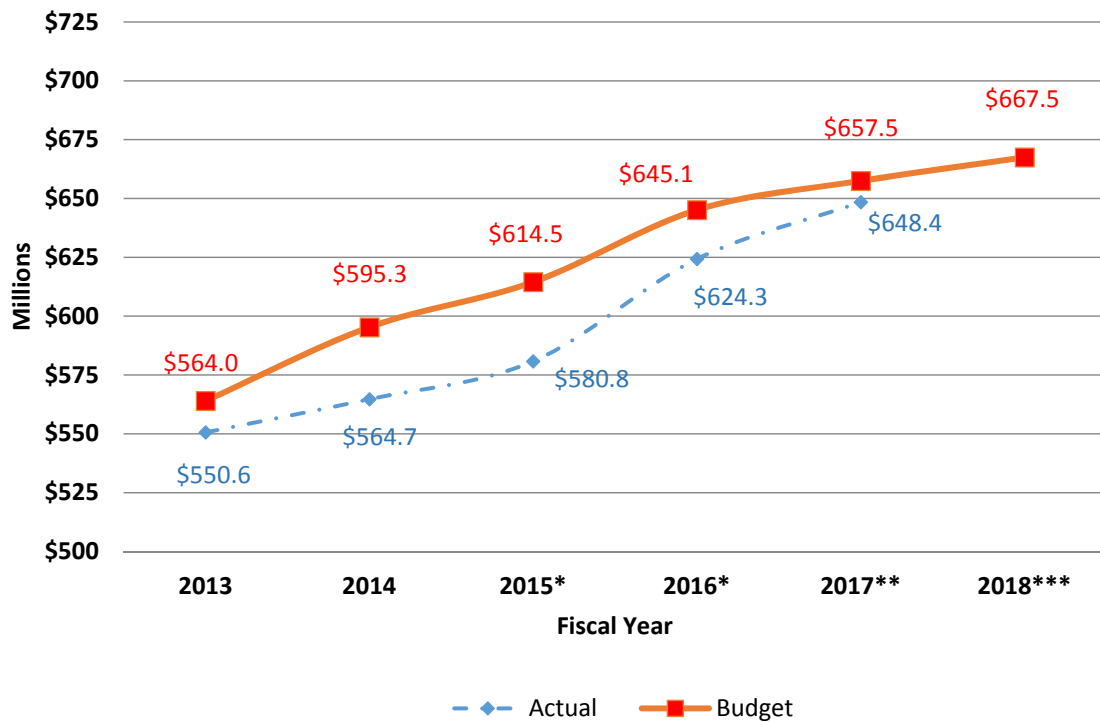
Source: City of Dallas Adopted Annual Budgets and FY 2017-18 Proposed Annual Budget (Unaudited)

Water Utilities Revenues

The Department of Dallas Water Utilities' (DWU) revenues are obtained through the sale of water and wastewater services in five customer classes: Residential, General Service, Municipal, Optional General Service, and Wholesale. The Wholesale customer class is comprised of 23 communities outside the City which receives treated water service and 11 communities which receive wastewater service. Rates for each class are determined by a cost of service study that assigns costs to each customer class based on DWU's cost to provide these services.

Chart IV

**Water Utilities Revenues
Analysis of Actual and Budget
FY 2013 to FY 2018**



* FY 2015 and FY 2016 Actual Revenues included \$ 6.8 M and \$13.4 M contributed capital assets from developers, respectively.

** FY 2017 revenues, including estimates for the remaining months, were provided by City management.

*** FY 2018 is proposed; therefore, actual is not available.

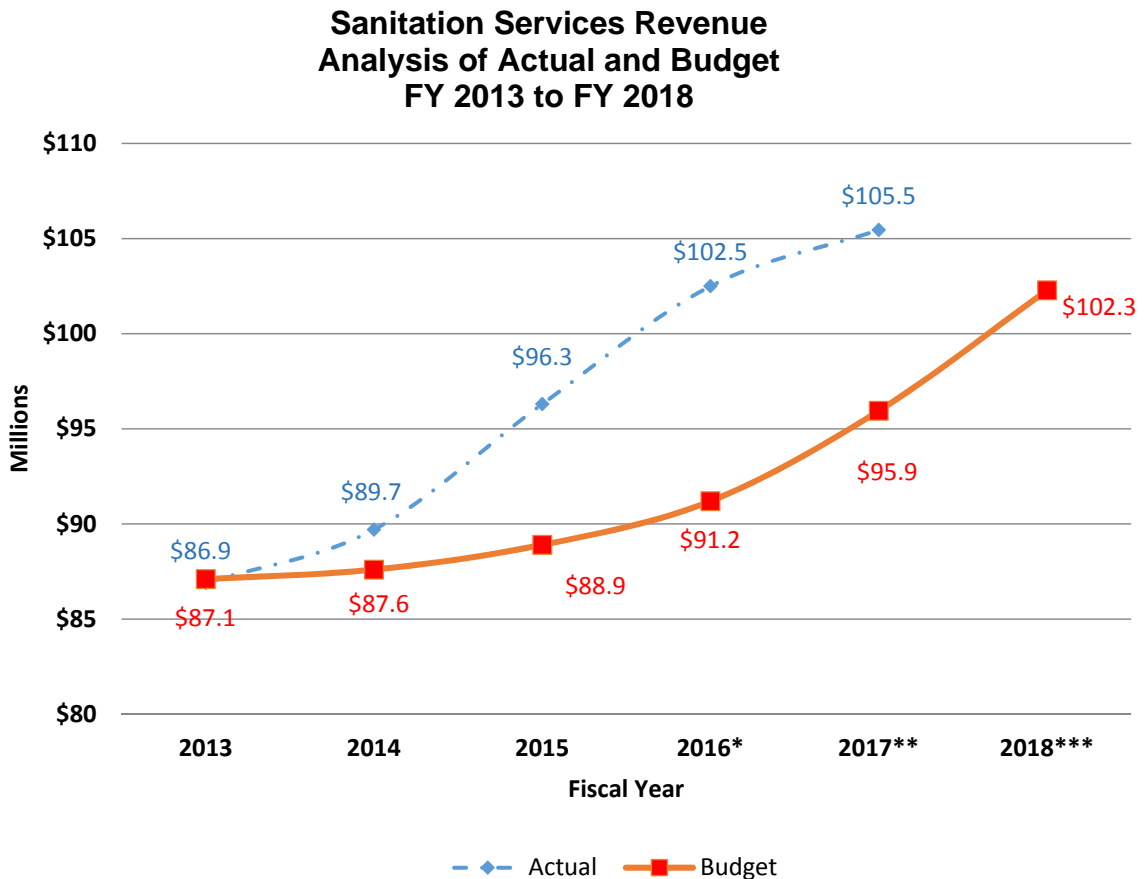
Source: City of Dallas Adopted Annual Budgets and FY 2017-18 Proposed Annual Budget (Unaudited)

Sanitation Services Revenue

Sanitation Services revenue is collected to match the cost of providing garbage collection, brush and bulky collection, and recyclables collection services for residential customers and a few small commercial customers. This revenue is based on fees, which are collected through the monthly water bills issued by DWU. In addition, fees are charged to non-Dallas residents and commercial waste haulers for disposing of solid waste at the McCommas Bluff Landfill and the Northwest (Bachman) Transfer Station.

The Department of Sanitation Services converted to an Enterprise Fund in FY 2015-16. According to management, after conversion of two revenue sources, the McCommas Site Rental and Commercial Container Fee will remain in the General Fund.

Chart V



* FY 2016 Adopted Budget was \$87,188,361. According to the FY 2016-17 Financial Summaries, the FY 2016 Adopted Budget was \$91,188,361. The Office of Financial Services stated that the increase of approximately \$4.0 million was due to the mid-year appropriation adjustment

** FY 2017 revenues, including estimates for the remaining months, were provided by City management.

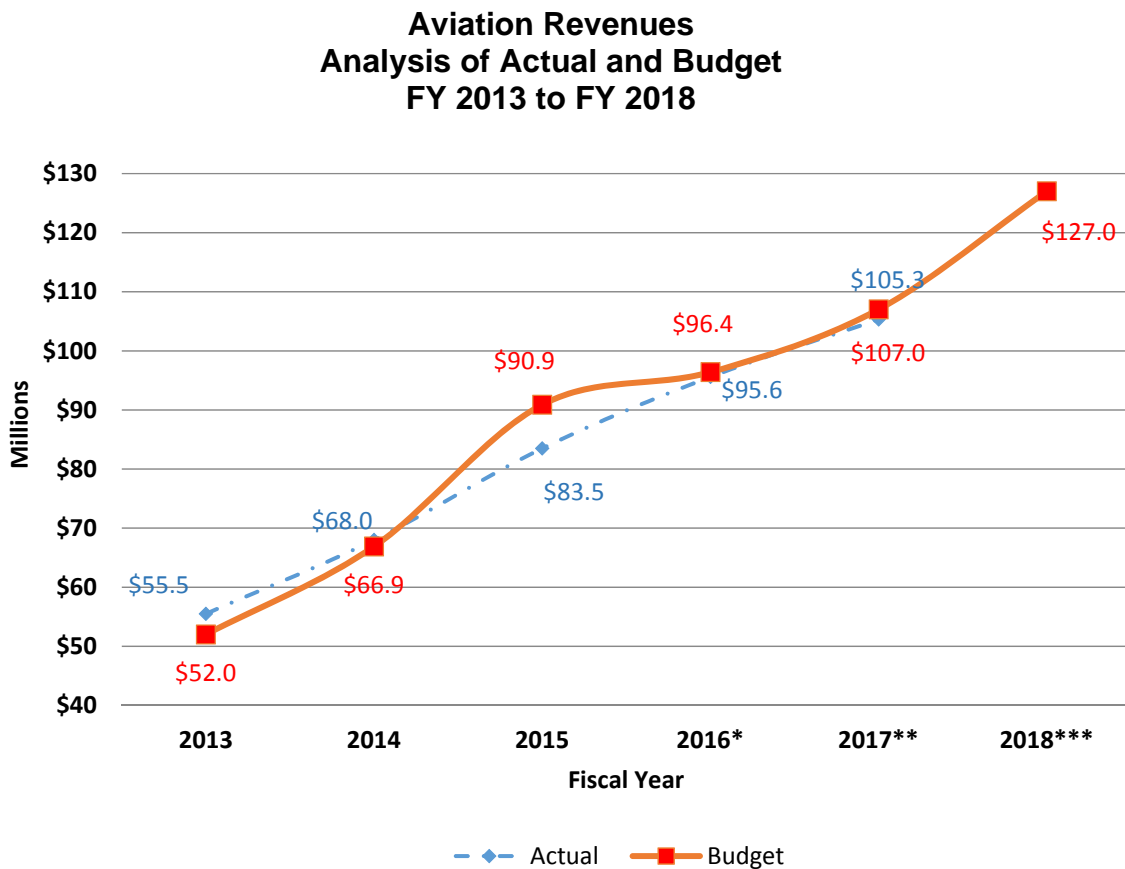
*** FY 2018 is proposed; therefore, actual is not available.

Source: City of Dallas Adopted Annual Budgets and FY 2017-18 Proposed Annual Budget (Unaudited)

Aviation Revenues

The Department of Aviation manages operations for both Dallas Love Field, Dallas Executive airports, and the downtown Vertiport. Revenues are comprised of landing fees, property rentals, and concessions. Airport businesses with concession contracts are obligated to pay the City a percentage of their monthly gross revenues or a guaranteed minimum payment. Concession ordinances include parking, food and beverage services, retail stores, advertising, car rental agencies, shoe shine services, and bag cart rental. Rental on Airport revenues are rental payments received from leased property at Dallas Love Field and Dallas Executive Airport. The leased property includes rent for airfield (ground) space, terminal building space, cargo building space, and associated shop and warehouse space.

Chart VI



* FY 2016 Adopted Budget was \$93,875,967. According to the FY 2016-17 Financial Summaries, the FY 2016 Adopted Budget was \$96,366,426. The Office of Financial Services stated that the increase of approximately \$2.5 million was due to the mid-year appropriation adjustment

** FY 2017 revenues, including estimates for the remaining months, were provided by City management.

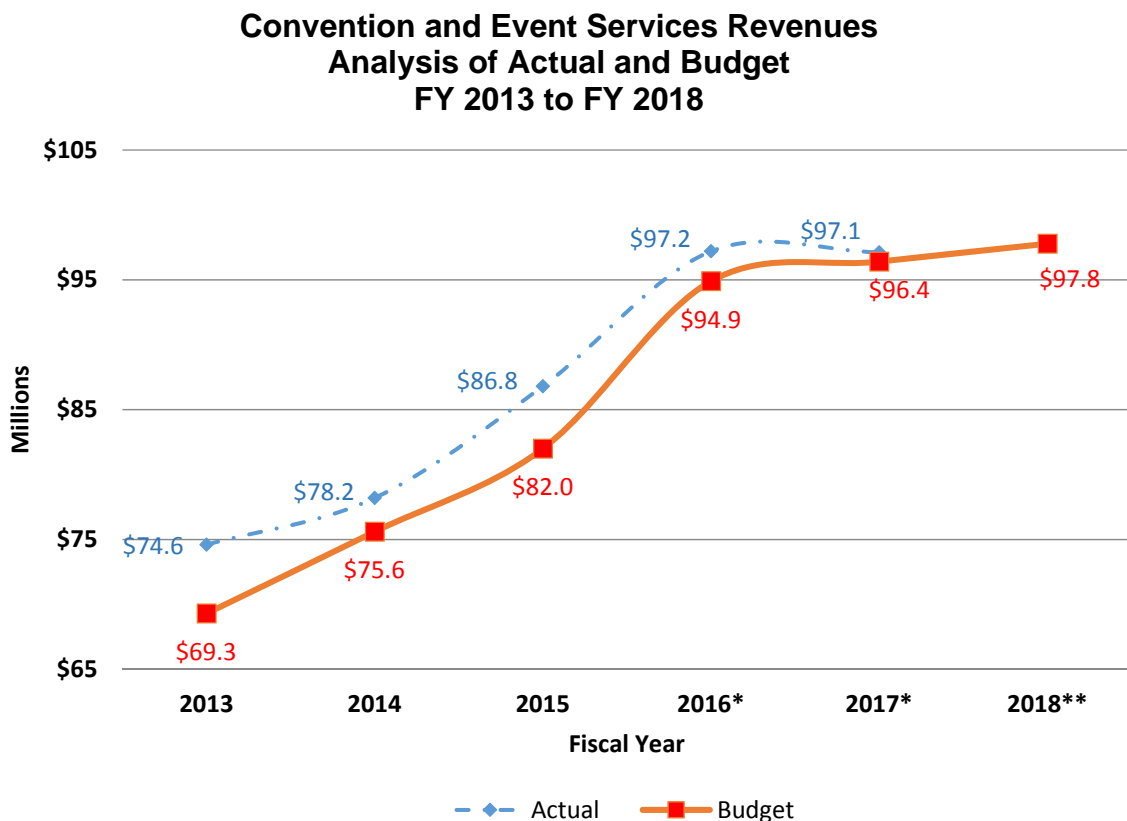
*** FY 2018 is proposed; therefore, actual is not available.

Source: City of Dallas Adopted Annual Budgets and FY 2017-18 Proposed Annual Budget (Unaudited)

Convention and Event Services Revenues

The major revenue source for the Department of Convention and Event Services (CES) is from the Hotel Occupancy Tax (HOT). The HOT rate in the City is 13 percent of the room rate charged within the City limits. The HOT is collected by the hotel at the point of sale and forwarded to the State (six percent) and to the City (seven percent) on a monthly basis. Of the seven percent, remitted to the City, approximately 30 percent is allocated to VisitDallas, formerly known as Dallas Convention and Visitors Bureau (DCVB), to market and promote the City as a convention and tourist destination. Approximately 67 percent is allocated to the Kay Bailey Hutchison Convention Center to support operations and capital improvements and approximately three percent is allocated to the Office of Cultural Affairs to encourage, promote, and improve the arts. Other revenue sources for CES include Alcohol Beverage Tax, Operating Revenues, and the Office of Special Events.

Chart VII



* FY 2016 Adopted Budget was \$83,996,067. According to the FY 2016-17 Financial Summaries, the FY 2016 Adopted Budget was \$94,896,067. The Office of Financial Services stated that the increase of approximately \$10.9 million was due to the mid-year appropriation adjustment.

** FY 2017 revenues, including estimates for the remaining months, were provided by City management.

*** FY 2018 is proposed; therefore, actual is not available.

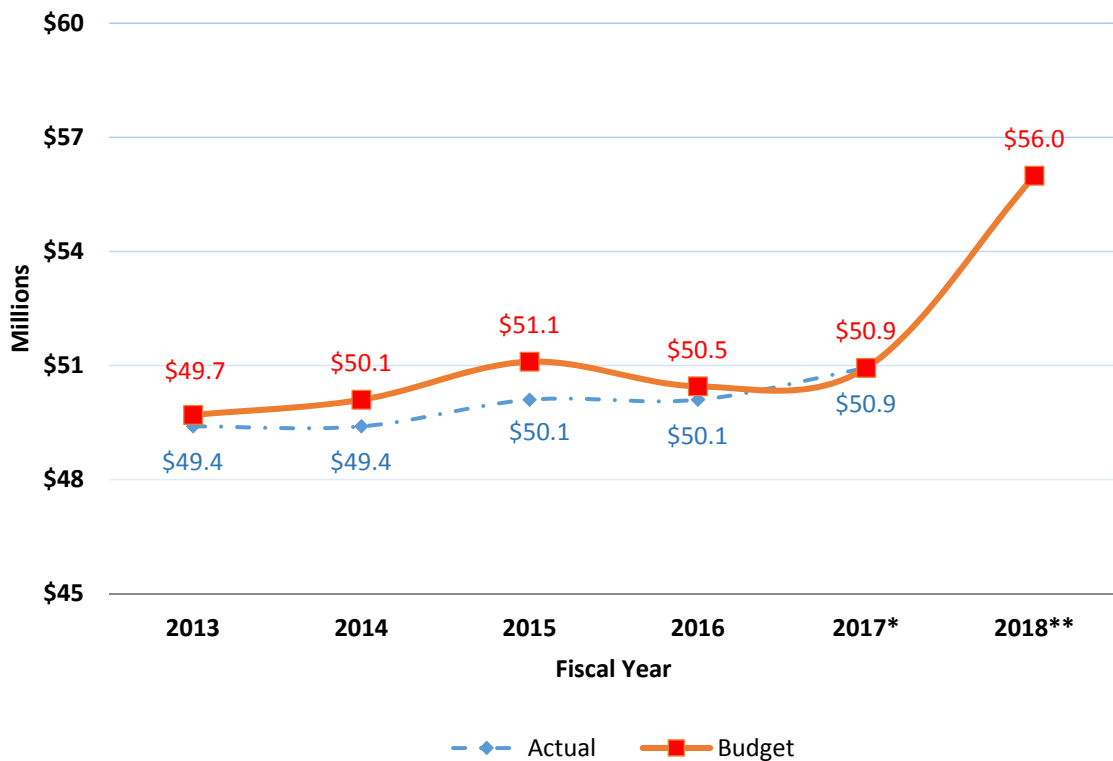
Source: City of Dallas Adopted Annual Budgets and FY 2017-18 Proposed Annual Budget (Unaudited)

Storm Water Fees Revenue

The Storm Water Drainage Management Utility revenue is collected to support the cost of operating and maintaining the City’s storm sewer system; maintenance of creeks, rivers and levees; monthly sweeping of the City’s major thoroughfares; water quality activities required by storm water permit (e.g., sampling, testing, monitoring, public education, and hazardous spill cleanup and disposal); and, engineering, design, and inspection of storm sewer infrastructure. Utility fees are billed and collected through the monthly water bills.

Chart VIII

**Storm Water Fees Revenue
Analysis of Actual and Budget
FY 2013 to FY 2018**



* FY 2017 revenues, including estimates for the remaining months, were provided by City management.
 ** FY 2018 is proposed; therefore, actual is not available.
Source: City of Dallas Adopted Annual Budgets and FY 2017-18 Proposed Annual Budget (Unaudited)