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LTC NO. 152-2008

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LETTER TO COMMISSION

TO: Mayor Matti Herrera Bower and Members of the City Commission

FROM: Jorge M. Gonzalez, City Manager

DATE: June 3, 2008

SUBJECT: Analysis of Building Fee Revenues

This letter summarizes an analysis of building/development process fees and expenses based on direction from the Commission at the February 13th 2008 Commission meeting.

Background

The preliminary actual revenue and expenses for the Fiscal Year ending September 30, 2007 was presented to the Commission at the February Commission meeting. The year-end budget to preliminary actual comparisons for the General Fund overall, showed an operating budget surplus of $15,504,725 (6.5%) in the General Fund, primarily due to the following:

1. Anticipated pro-active cost-saving measures implemented very early in the Fiscal Year in association with property tax reform legislation (approximately $4.6 million Citywide);
2. Approximately $4.4 million in additional revenues were anticipated in the FY 2006/07 third quarter projections that were included in the FY 2007/08 Proposed Budget book primarily due to increased electrical franchise fees, police and fire off-duty fees, Miami Beach Golf Course revenues, as well as increased interest earnings due to higher than budgeted interest rates and fund balances, increased rent and lease revenues due primarily to the new Live Nation agreement, and increased building permit revenues - these increases were partially offset by reduced ad-valorem property taxes primarily due to higher than anticipated property value appeals approved by Miami-Dade County; and
3. Over $6 million due to the implementation of new processes and a comprehensive review of open permits due to certain inconsistencies in the application of building permit fees in the City.

Pursuant to Resolution 2008-26771, the Commission approved the use of the $15 million surplus to fund the City's capital reserve, Replace Capital Investment Upkeep Account funds that were reduced in FY 2007/08 budget pursuant to the second budget hearing, reimburse the City's FY 2007/08 operating contingency as included in the resolution adopting the City's Education Compact for International Baccalaureate implementation costs, replace Convention Development Taxes (CDT) funds used for Lincoln Road improvements and construction of the new Fire Station 2 based on the recent Miami-Dade County audit, reduce deficits in the City's Risk Management Fund pursuant to the City's financial policy, and consistent with direction received in the preparation of the City's FY 2007/08 Annual Operating Budget, and to continue to set aside funds for the City's accrued liability for postemployment (retiree health) benefits. However, based on concerns expressed at the meeting, this approval was subject to a review of building/development process revenues and expenses to ensure that Building/development revenues were being used only for building/development expenses.

In 2003 JRD & Associates (JRD) conducted an analysis of the Department's fees, incorporating the results of a cost allocation that was performed by KPMG for FY 1998/99. The attached letter from JRD summarizes the updated analysis requested at the February meeting, updating the results of our 2003 analysis through FY 2007/08. This is not a new study but just an update of their 2003 analysis.

Analysis Summary

In comparing revenues to expenses, JRD analyzed building/development process related revenues and both direct Building Department Costs as well as the cost allocation of support and indirect expenses - those incurred by other City departments in providing resources that allow the Building Department to perform its duties.

Support and indirect costs are based on the KPMG study in FY 1998/99, at which time these expenses represented 40% of direct Building Department expenses. In 2003, JRD calculated the average ratio of Support and Indirect Expenses to actual expenses for FY 1998/99 through FY 2001/02 to be 34% based on an assumption that Support and Indirect Expenses increased by 8% annually since 1998/99, similar to the increase in the General Fund Current Service Level (CSL) over time. However, using the 8% increase per year results in support and indirect cost of only 24% of direct Building Department expenses by FY 2006/07 – a very conservative estimate of indirect support costs.

Based on the range of possible support and indirect cost assumptions, the analysis shows the Building Department "owing" the General Fund $1.4 million based on the 24% factor by FY 2006/07, or the General Fund "owing" the Building Department $3.9 million with the 40% factor. The recommended approach by JRD is to maintain the 34% assumption used in the prior study which results in the cumulative carry-over for the Building Department of $911,483 over the last six years, primarily due to the $6 million recovered by the City in FY 2006/07 as a result of the comprehensive review of open permits that represents multiple years of historical revenues collected in this one year. Had this unusual revenue increase not occurred, building permit fee revenues versus expenditures would have been short by approximately $3.2 million in FY 2006/07, resulting in a cumulative deficit of $5.1 million between FY 2002/03 actuals and the FY 2007/08 budget.

The analysis also identified concerns that the KPMG cost allocation study was conducted ten years ago, and may no longer be accurate with respect to the City agencies providing support to the Building Department, especially as significant departments such as Public Works, Code Enforcement and Planning and Zoning costs did not have expenses allocated to the Building Department.

Recommendation

It is recommended that no changes be made at this time to the appropriation of FY 2006/07 surplus funds as approved by the Commission in February. Rather, it is recommended that a comprehensive update to the FY 1998/99 KPMG allocations study be performed as part of a larger Building permit fee study and that the approximately $1 million identified above should be held aside in the Capital Reserve Fund until the study is completed.

Further, although the new processes recently implemented have resulted in more appropriate levels of permit fee revenues, in the longer term, it is recommended that we review our fee structure entirely. Building staff, as well as outside consultants, have observed that our fee structure is more complicated than in other jurisdictions.

As a result, I recommend engaging in an RFP process to select a consultant to provide recommendations of revised fee structures and levels. The RFP would include update studies of direct as well as support and indirect costs related to the building/development process, and provide relevant and realistic recommendations appropriate fee levels and structure for building/development permit fees. As part of the indirect and support analysis, the consultant would review the FY 2006/07 direct/support and indirect costs versus revenues related to all departments involved the City's building development process to determine if there was a shortfall or surplus during that year as well as provide an interpolation for the intervening years since the last cost allocation study was performed in FY 1998/99.

Once the study is complete, it is further recommended that an updated analysis of building/development process revenues and expenses be performed at each fiscal year-end in the future.

I hope to include the proposed RFP at the June 2008 Commission meeting.

Attachment

JMG/KGB

JRD & associates, inc.
Industrial Engineers • Management Consultants

May 22, 2008

Ms. Kathie Brooks
Director
Office of Budget and Performance Improvement
City of Miami Beach
1700 Convention Center Drive
Miami Beach, FL 33139

Dear Ms. Brooks:

Per your request, the following is an analysis detailing the carry-over or deficit incurred by the City's Building Department since Fiscal Year (FY) 2002/03. As you will recall, in 2003 JRD & Associates conducted an analysis of the Department's fees. At that time, we incorporated the results of a cost allocation that was performed by KPMG for FY 1998/99. The purpose of this analysis is to update the results of our 2003 analysis through FY 2007/08. This is not a new study but just an update of our 2003 analysis. The figures are based on the financial reports published in the City's adopted budget documents and are summarized in Table 1 below.

The components below (Table 1) consist of all building permit related revenues, including:

- Permits – Building
- Permits – Electrical
- Permits – Elevator Inspection
- Permits - Mechanical
- Permits – Plumbing
- Certificate of Occupancy
- Certificate of Completion
- Permits – Building Recertification
- Permits – Demolition
- Microfilm – Building Department
- Reimbursement – Radon
- Building Code Violations
- Building Training Surcharge
- Building - Other

Additionally, below are listed Department expenses, consisting of Salaries and Benefits, Operating Expenses, Internal Service Charges, and Capital, as well as the cost allocation of support and indirect expenses - those incurred by other City departments in providing resources that allow the Building Department to perform its duties (e.g. – City Manager's Office, City Attorney's Office, City Clerk, etc.).

These expenses were calculated by KPMG in its FY 1998/99 study, and have not been recalculated since. As such, JRD & Associates calculated the average ratio of Support and Indirect Expenses to actual expenses for FY 1998/99 through FY 2001/02 (based on the previous JRD & Associates study) to be 34%, and applied this percentage to the actual expenses for FY 2002/03 through FY 2007/08 to determine the appropriate Support and Indirect Expenses (i.e. – for FY 2002/03, Support and Indirect Expenses = ($4,192,211 * .34).

At the time JRD & Associates performed its 2003 analysis, an assumption was made that Support and Indirect Expenses increased by 8% annually, similar to the increase in the General Fund Current Service Level (CSL) over time. At the time of the KPMG study in FY 1998/99, indirect expenses represented 40% of direct Building Department expenses. Using the 8% increase per year would result in an indirect increase by FY 2006/07 of only 24% of direct Building Department expenses – a very conservative estimate of indirect support costs, and would result in the General Fund "owing" the Building Department $3.9 million. Conversely, using a 40% factor of indirect costs each year would result in the Building Department "owing" the General Fund $1.4 million.

More importantly, the KPMG cost allocation study that was conducted ten years ago has not been revised and may no longer be accurate with respect to the City agencies providing support to the Building Department. For example, at the time of the study, Public Works, Code Enforcement and Planning and Zoning costs were not been allocated to the Building Department and should be since these departments are part of the development process.

None-the-less, in order to provide a reasonable order of magnitude estimate of the cost of indirect support provided to the Department from other City agencies, the aforementioned ratio (average) of 34% is believed to be the more reasonable approach. The resulting analysis is provided below.

Table 1

Fiscal Year	Revenues	Expenses	Support and Indirect Expenses	Total Expenses	Annual Carry-Over / Deficit	Cumulative Carry-Over / Deficit
02-03	$5,672,160	$4,192,211	$1,425,352	$5,617,563	$54,597	$54,597
03-04	$6,933,074	$4,878,194	$1,658,586	$6,536,780	$396,294	$450,891
04-05	$8,247,818	$5,585,758	$1,899,158	$7,484,916	$762,902	$1,213,793
05-06	$9,361,357	$6,688,069	$2,273,943	$8,962,012	$399,345	$1,613,138
06-07	$13,252,651	$7,805,184	$2,653,763	$10,458,947	$2,793,704	$4,406,842
07-08 *	$8,148,425	$8,689,391	$2,954,393	$11,643,784	- $3,495,359	**$911,483**
Total	**$51,615,485**	**$37,838,807**	**$12,865,195**	**$50,704,002**	**$911,483**	**N/A**

* Budget

As you can see, over the last six years, the cumulative carry-over for the Building Department has been approximately $911,483. This is due primarily to the $6 million recovered by the City in FY 2006/07 as a result of the permit fee audit conducted by the City's Audit Department that represents multiple years of historical revenues collected in this one year. Had this unusual revenue increase not occurred, building permit fee revenues versus expenditures would have been short by approximately $3.2 million in FY 2006/07, resulting in a cumulative deficit of $5.1 million from FY 2002/03 and FY 2007/08 budget.

I look forward to discussing this analysis with you at your convenience.

Sincerely,

Jorge R. Duyos

Jorge R. Duyos, P.E.