



## CITY OF SALINAS COUNCIL STAFF REPORT

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**DATE:** **FEBRUARY 20, 2018**

**DEPARTMENT:** **FINANCE**

**FROM:** **MATT N. PRESSEY, CPA, FINANCE DIRECTOR**

**TITLE:** **FY 2017-18 MID-YEAR BUDGET REVIEW AND BUDGET ADJUSTMENTS**

### RECOMMENDED MOTION:

A motion to accept the mid-year FY 2017-18 budget review reports, adopt a resolution approving amendments to the FY 2017-18 operating and capital budgets for the City of Salinas, and receive a status update on the Salinas Financial Sustainability Plan.

### RECOMMENDATION:

It is recommended that the City Council:

- 1) Accept the mid-year FY 2017-18 budget review reports; and
- 2) Adopt a resolution approving amendments to the FY 2017-18 operating and capital budgets for the City of Salinas.
- 3) Receive a status update on the Salinas Financial Sustainability Plan

### EXECUTIVE SUMMARY:

The City moves into this mid-year with a keen eye on the future and the actions that must be taken today to manage the future. At mid-year, revenues are coming in as expected and expenditures are on budget, except for the Fire Department, which is expected to be over budget. The mid-year review includes a variety of budget adjustments. The mid-year review also includes a discussion on how to remedy the Fire Department over budget situation. The future outlook shows healthy resources, however, the trajectory of forecasted expenditures will far outpace the revenue growth unless changes can be put in motion now.

### BACKGROUND:

One year ago in February 2017, at the last mid-year review, staff presented the Salinas Financial Sustainability Plan Framework (Sustainability Plan) for the first time. Staff began the Sustainability Plan in August 2016 with the goal to eliminate the structural deficit of the General Fund. The effort began with meetings held in every department to inform them of the structural

deficit and the goal to resolve it. Department staff were solicited for ideas aimed at generating new revenues and cutting or saving on costs. Two significant fiscal impact items occurred between August 2016 and the February 2017 mid-year review: 1) The Salinas Police Officers Association (SPOA) three year Memorandum of Understanding (MOU) was approved (September 2016; \$11.7 million cumulative cost increase over three years) and 2) CalPERS lowered the discount rate (December 2016; \$70.9 million cumulative cost increase over 7 years, with the total annual cost doubling by the seventh year). The increase in cost from the CalPERS discount rate change and the SPOA MOU is likely the largest fiscal impact in the City's History.

What began as a manageable effort to eliminate the General Fund Structural Deficit in August 2016 has become the most challenging task, similar to the great recession, where revenues had dropped off significantly and the City eliminated 135 positions or 20% of the City's workforce. Over the next seven years, although phased in, the impact of the PERS discount rate is a looming tsunami that will require serious planning and rethinking of priorities and service delivery.

The City Manager has been holding monthly budget meetings with the department heads to collaborate on the strategies, implementation of the Sustainability Plan, and on tough decisions and recommendations that need to be brought forward to City Council.

#### DISCUSSION:

##### **Mid-Year Review and Budget Adjustments**

###### *Revenue*

At mid-year, the General Fund revenues are coming in as expected. As of December 31, 2017, the City received \$49,196,556, or 52% of the budget, as shown in the table below. The five major revenues, representing 91% of all General Fund Revenues, are coming in on budget and are projected to end the year right on budget, so no mid-year adjustments are proposed for these top five revenues. As part of the mid-year review, staff is recommending increasing the estimated revenue by \$125,000 for cannabis related service fees.

	<b>Adopted</b>			<b>Proposed</b>		
	<b>Budget</b>	<b>Actual</b>	<b>Difference</b>	<b>% Rec.</b>	<b>Adjustments</b>	
Sales Tax	\$ 28,637,500	\$ 15,006,904	\$ 13,630,596	52%	\$ -	
Property Tax	28,029,000	15,502,310	12,526,690	55%	-	
Utility Users Tax	12,200,000	6,184,674	6,015,326	51%	-	
Franchise Fees	8,689,000	4,044,964	4,644,036	47%	-	
Business License Tax	4,900,000	1,171,911	3,728,089	24%	-	
All Other	<u>11,285,200</u>	<u>7,285,793</u>	<u>3,999,407</u>	65%	<u>125,000</u>	
<b>Total Revenue</b>	<u><b>\$93,740,700</b></u>	<u><b>\$49,196,556</b></u>	<u><b>\$44,544,144</b></u>	<b>52%</b>	<u><b>\$ 125,000</b></u>	

For a detailed revenue report of the above information, please see Exhibit D.

### Operating Expenditures

Operating Expenditures of the General Fund are under budget mid-way through the year. The General Fund total expenditures was \$48,164,101 as of December 31, 2017, or 49% spent. Mid-year adjustments to the operating budget totaled \$716,125 and are detailed in Exhibit A to this staff report.

	Adopted		Difference	% Spent	Proposed	
	Budget	Actual				Adjustments
Police	\$ 39,765,516	\$ 18,025,982	\$ 21,739,534	45%	\$ 16,125	
Fire	19,692,662	11,545,286	8,147,376	59%	50,000	
Public Works	10,250,432	4,833,051	5,417,380	47%	-	
Library & Com. Serv.	921,435	379,676	541,759	41%	-	
Community Dev.	3,071,929	1,331,025	1,740,904	43%	-	
Administration	3,362,303	1,425,511	1,936,793	42%	125,000	
Finance	4,326,384	1,899,701	2,426,682	44%	20,000	
City Attorney	1,034,870	498,706	536,164	48%	25,000	
City Council	202,460	122,056	80,404	60%	-	
Non-Dep.	7,200,135	4,146,807	3,053,328	58%	480,000	
Non-Dep.-Trans Out	<u>8,132,910</u>	<u>3,956,299</u>	<u>4,176,611</u>	<u>49%</u>	<u>-</u>	
<b>Total Operating Exp.</b>	<b><u>\$97,961,035</u></b>	<b><u>\$48,164,101</u></b>	<b><u>\$49,796,934</u></b>	<b><u>49%</u></b>	<b><u>\$ 716,125</u></b>	

Staff has projected the Fire Department's expenditures through the rest of the fiscal year and project the Fire Department will be approximately \$500,000 over budget after factoring in out of county revenue reimbursements. The main cause of the over budget condition is minimum staffing and the amount of overtime incurred above the normal budget for vacant positions. There are many options to help remedy this condition that can be implemented at mid-year. Staff are discussing the alternatives and plan to implement a solution as soon as possible.

### Capital Improvement Program (CIP) Expenditures

The total CIP budget of \$90,400,135 includes \$34,906,130 budgeted as part of the FY 2017-18 adopted budget and \$55,494,005 of projects in progress where the budget carries over year-to-year until completed. Year-to-date CIP expenditures totaled \$9,727,597 and encumbrances totaled \$12,899,553 as of December 31, 2017. Mid-year adjustments to the CIP budget total \$796,100 and includes \$150,000 from the General Fund for City-wide clean-ups, \$620,000 from Measure X funded projects, and \$26,100 from Measure G funding, as described in detail in Exhibit A to this staff report.

<b>CIP By Dept.</b>	<b>Budget</b>	<b>Actual</b>	<b>Encumb.</b>	<b>Difference</b>	<b>Spent &amp; Enc.</b>	<b>Proposed</b>	
						<b>%</b>	<b>Adjustments</b>
Police	\$ 15,097,422	\$ 1,150,389	\$ 3,413,258	\$ 10,533,775	30%	\$ -	-
Fire	3,375,019	581,279	337,586	2,456,154	27%		-
Public Works	57,828,894	6,563,779	6,936,966	44,328,149	23%	770,000	
Library & Com. Serv.	5,910,556	668,267	1,583,519	3,658,771	38%	26,100	
Community Dev.	3,844,209	391,246	567,642	2,885,322	25%		-
Administration	3,658,126	98,938	8,600	3,550,588	3%		-
Finance	685,908	273,698	51,982	360,228	47%		-
<b>Total CIP</b>	<b>\$90,400,135</b>	<b>\$ 9,727,597</b>	<b>\$12,899,553</b>	<b>\$67,772,985</b>	<b>25%</b>	<b>\$ 796,100</b>	

	<b>Proposed</b>
	<b>Adjustments</b>
Measure X	\$ 620,000
Measure G	26,100
General Fund	150,000
<b>Total CIP Adjustments by Funding Source</b>	<b>\$ 796,100</b>

### Measure E

The Measure E Committee met on January 18, 2018. They reviewed the status of the FY 2017-18 operating and capital projects funded with Measure E. To date, there was a total of \$5,644,795 in operating expenditures spent and \$6,567,766 was collected in revenue. Please see the attached “10-Exhibit H - December 31, 2017 Measure E Financial Report” for more details.

### Measure G

The Measure G Committee met on January 25, 2018. They reviewed the status of the FY 2017-18 operating and capital projects funded with Measure G. To date, there was a total of \$9,370,448 spent and \$13,227,286 was collected in revenue. Please see the attached “8-Exhibit F - December 31, 2017 Measure G Financial Report” for more details.

Also included as an attachment to this report is the status of Measure G funded projects. The report is titled, “9-Exhibit G - December 31, 2017 Measure G Funded CIP Projects”. The Measure G funded capital project report shows \$2,113,207 spent, or 9% of the budget and \$18,512,525 spent life-to-date (LTD) as of December 31, 2017. The following table summarizes the Measure G funded CIP activity for the first six months of the year by department:

## Measure G CIP

Department	FY 2017-18				Total (LTD)	
	Budget	Actual Exp.	Balance	Spent	%	Actual Exp.
12 - Administration	\$ 50,000	\$ -	\$ 50,000	0%	\$ 254,846	
20 - Finance	249,251	124,972	124,279	50%	1,696,221	
30 - Community Development	1,369,862	76,330	1,293,532	6%	996,304	
40 - Police	14,296,687	781,370	13,515,317	5%	4,521,776	
45 - Fire	2,326,061	535,334	1,790,727	23%	3,200,181	
50 - Public Works	3,609,669	484,294	3,125,375	13%	6,906,683	
55 - Community Services	1,230,365	110,907	1,119,458	9%	936,514	
Total	<u>\$ 23,131,895</u>	<u>\$ 2,113,207</u>	<u>\$ 21,018,688</u>	9%		<u>\$ 18,512,525</u>

As mentioned above, the detailed list of Measure G funded CIP projects are included as an attachment to this report.

### Investment Activity

Cash and Investments total \$130,365,373. The General Fund totals \$24,588,048 or 18.86% of the total portfolio. Please see, "Exhibit B – Summary of Cash and Investments" as of December 31, 2017. It shows that the City has sufficient liquid funds to meet its cash requirements for at least the next six months. The Financial Report includes all investment detail required by SB564 (Johnston) and is presented to Council in compliance with the City's investment policy.

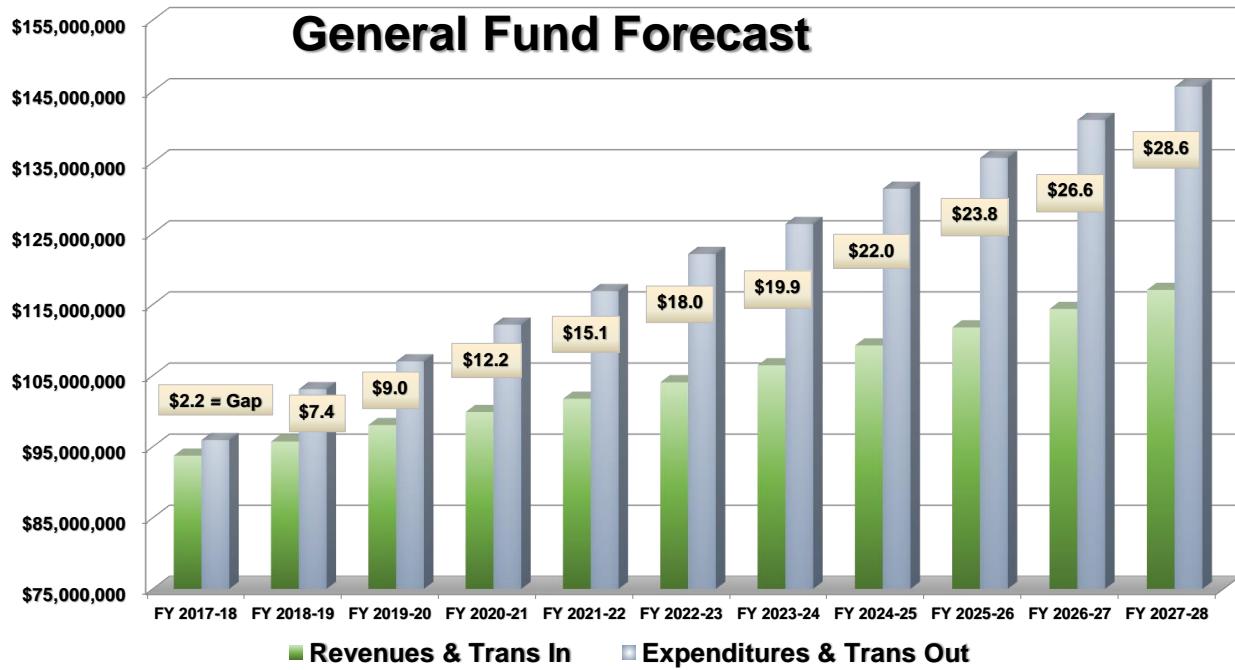
### Cash Balances

The Housing and Urban Development Fund has a deficit of \$557,384 and will be cleared when revenues are received from various HUD grants. The Downtown Parking District Fund has a deficit of \$1,032,908 which will be covered by the General Fund until the Comprehensive Downtown Parking Study Plan is completed and implemented. Please see, "Exhibit C – Statement of Cash Balances – All Funds".

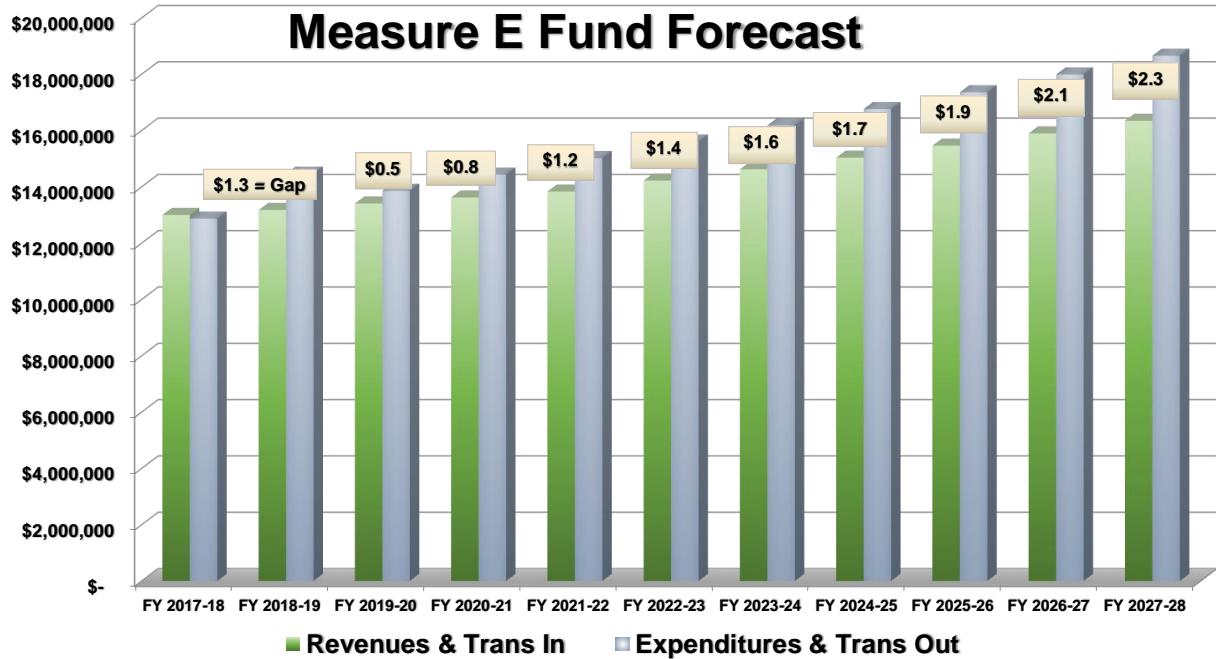
### Fiscal Forecast and Sustainability Plan

#### Fiscal Forecast

The General Fund Forecast has been refreshed, which takes into consideration the existing operating programs and their full cost. It also refreshes the revenue forecasts with the most recent historic trends and information on new development and improvement of property and retail establishments. With salary and benefits representing 80% of the General Fund budget, the main cost drivers are, of course, salary, retirement, and health care. The gap between revenue and expenditures over the next ten years are shown and discussed below.



In the General Fund alone, during the next 10 years, total expenditures are projected to increase by an average of \$5.5 million per year, or 4.3%. Total revenue, on the other hand, is projected to increase an average of \$2.3 million, or 2.2%. Salaries are projected to increase by an average of \$1.5 million a year, or 3%. PERS cost are projected to increase an average of \$1.5 million per year, or 7.3%. The structural deficit grows an average of \$2.6 million per year, or 29.3%.



In the Measure E Fund alone, during the next 10 years, total expenditures are projected to increase by an average of \$578,000 per year, or 3.8%. Total revenue, on the other hand, is projected to increase an average of \$335,000, or 2.3%. Salaries are projected to increase by an average of \$200,000 a year, or 2.7%. PERS cost are projected to increase an average of \$139,000 per year, or 7.0%. The projected deficit grows an average of \$244,000 per year, or 31.2%. The projections above currently exclude the additional debt service payment of around \$850,000 to fund the El Gabilan Library expansion. The current plan to fund the El Gabilan Library includes freezing certain positions through attrition until the future growth impact fees begin to come in.

At the inception of Measure G, the full 15-year term of Measure G had been projected with a mix of operating and capital items that restore services and enhance capital needs in the community. The 10-year projections for Measure G are balanced between revenue and expenditures. The one-time capital expenditures are the mechanism to adjust to maintain balance each year.

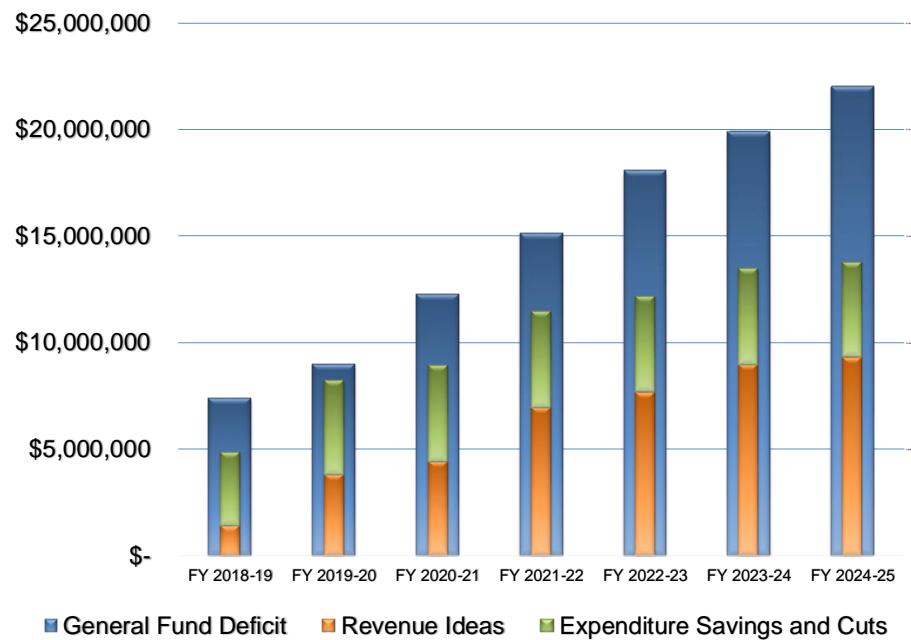
### Sustainability Plan

The Sustainability Plan serves as a tool to manage the structural deficit and work toward eliminating it. The major items in the plan are listed below and are in progress to being fully developed and implemented:

- **Cal PERS and 115 Trust Option**
  - The City is working on contracting with a 115 Trust service provider
  - A 115 Trust will be established to fund and stabilize the future impacts of the PERS discount policy changes
  - The RFQ was issued
  - 4 submissions
  - Evaluation team narrowed the selection down to two finalists
  - Interviews conducted Friday, February 16, 2018
  - Recommendations will be brought back to City Council on March 20, 2018
- **Center for Public Management (CPSM) Study**
  - This study focuses on police and fire deployment through the study of service calls and overtime with the goal of becoming more efficient and reducing cost
  - Public safety is the largest cost for the City and the highest priority; As the largest cost, the sustainability plan must include service delivery of public safety
- **National Resource Network (NRN) Study**
  - Reviewing all departments and all costs of the City of Salinas
  - Developing a 10 year model for the General Fund, Measure E, and Measure G
  - Preliminary base 10 year model has been developed and is included as figures in this report

- NRN will assist with recommendations on how to balance the structural deficit and build “what-if’s” into the 10 year model to assist with measuring the future impact of the “what-if” scenarios
- **Storm Water Fee Study and Fee Implementation**
  - Has the potential to generate \$2 million in revenue to fund the unfunded Federal clean water mandate
- **Cannabis**
  - Has potential to generate \$3 million a year in revenue over time.

The sustainability plan currently has 17 revenue generating ideas and 55 cost cutting ideas that are being monitored or worked on. With the refreshed General Fund Forecast, the table and graph below shows the impact the new revenue and expenditure saving items can have on the structural deficit during the next 7 years.



	FY 2017-18	FY 2018-19	FY 2019-20	FY 2020-21	FY 2021-22	FY 2022-23	FY 2023-24	FY 2024-25	Total
General Fund Deficit	(1,152,847)	(7,378,167)	(8,956,642)	(12,276,476)	(15,139,706)	(18,038,312)	(19,866,529)	(22,027,890)	(104,836,568)
New Revenue	1,007,600	1,394,600	3,783,600	4,410,600	6,955,600	7,670,900	8,977,700	9,286,700	43,487,300
Expenditure Savings and Cuts	2,163,100	3,472,900	4,436,100	4,502,600	4,502,600	4,486,400	4,486,400	4,486,400	32,536,500
	2,017,853	(2,510,667)	(736,942)	(3,363,276)	(3,681,506)	(5,881,012)	(6,402,429)	(8,254,790)	(28,812,768)

The key to success in eliminating the structural deficit will be in execution. All departments will need to work hard to implement the revenue generating and cost savings ideas. Furthermore, it is important to continue to control costs going forward, especially with CalPERS considering lowering the discount rate further, MOU's that will be expiring soon and the potential of a downturn in the economic cycle.

## Reserves

The City's Financial Policies provide that the City "strive" to maintain an eight (8%) percent General Fund Operating Reserve. Five (5%) percent of the reserve is required primarily for cash flow purposes. Reserves above the five (5%) percent level can be characterized more as "rainy day" funds to guard against economic uncertainties.

While a prudent reserve is certainly a worthy policy, it must be balanced with the fact that residents pay taxes for one purpose – to benefit from programs and services paid for with those taxes.

During the Great Recession, the FY 2009-10 Budget was balanced using \$9.4 million of General Fund/Measure E reserves. The use of reserves in both FY 2008-09 and FY 2009-10 was required to maintain services and were depleted to zero. Over the last six fiscal years using carryover funds and at the mid-year budget review, the City Council has approved replenishing the reserve with amounts each time. The General Fund, Measure G and E reserves have grown and are now at \$9.6 million or 8.9% of operating expenditures. The Measure G reserve of \$1,760,000 is 8% of the 1st year estimated Measure G sales tax of \$22,000,000 and will function both as an operating reserve and a capital reserve. In addition to these reserves, the City has reserved \$2,500,000 for the New York Life Retirement Reserve and \$1,300,000 remaining in the deficit reduction reserve.

Fund Balance Reserves:	<u>General Fund</u>	<u>Measure V</u>	<u>Measure G</u>	<u>Total</u>
Operating Reserve	\$ 6,830,000	\$ 962,000	\$ 1,760,000	\$ 9,552,000
Proposed Increase	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total Reserves	<u><u>\$ 6,830,000</u></u>	<u><u>\$ 962,000</u></u>	<u><u>\$ 1,760,000</u></u>	<u><u>\$ 9,552,000</u></u>
Reserve % of FY 17-18 Appropriations	7.7%	8.0%	13.8%	8.4%

## CEQA CONSIDERATION:

Not a Project. The City of Salinas has determined that the proposed action is not a project as defined by the California Environmental Quality Act (CEQA) (CEQA Guidelines Section 15378). In addition, CEQA Guidelines Section 15061 includes the general rule that CEQA applies only to activities which have the potential for causing a significant effect on the environment. Where it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment, the activity is not subject to CEQA. Because the proposed action and this matter have no potential to cause any effect on the environment, or because it falls within a category of activities excluded as projects pursuant to CEQA Guidelines section 15378, this matter is not a project. Because the matter does not cause a direct or foreseeable indirect physical change on or in the environment, this matter is not a project.

## STRATEGIC PLAN INITIATIVE:

Although the mid-year review and adjustments applies to all the strategic plan initiatives, the main Council goal is Effective, Sustainable Government.

## FISCAL AND SUSTAINABILITY IMPACT:

General				Permit	
	Fund	Measure G	Measure X	Parking	Center
<b>Mid-Year Budget Adjustments:</b>					
Revenue	\$ 125,000	\$ -	\$ -	\$ 269,400	
Appropriations	(716,125)	-	-	(269,400)	(126,682)
CIP	(150,000)	(26,100)	(620,000)	-	-

## ATTACHMENTS:

- Resolution - FY 2017-18 Mid-Year Budget Amendments
- Exhibit A - FY 2017-18 Mid-Year Budget Adjustments Detail
- Exhibit B - Summary of Cash and Investments
- Exhibit C - Statement of Cash Balances – All Funds
- Exhibit D - December 31, 2017 Revenue Report (General Fund, Measure E(V) and Measure G)
- Exhibit E - December 31, 2017 General Fund Expenditure Report
- Exhibit F - December 31, 2017 Measure G Financial Report
- Exhibit G - December 31, 2017 Measure G Funded CIP Projects
- Exhibit H - December 31, 2017 Measure E Financial Report
- Exhibit I - December 31, 2017 CIP Projects
- Exhibit J – December 31, 2017 Revenue Report - All Funds
- Exhibit K - December 31, 2017 Operating Expenditure Report By Program - All Funds