



Agenda Report

Fullerton City Council

MEETING DATE: FEBRUARY 18, 2020

TO: CITY COUNCIL / SUCCESSOR AGENCY

FROM: KENNETH A. DOMER, CITY MANAGER

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SUBJECT: SECOND QUARTER FINANCIAL REPORT AND MID-YEAR BUDGET AMENDMENTS FOR FY 2019-20

SUMMARY

The second quarter financial report provides an overview of the City's financial position through the second quarter (or first half) of Fiscal Year 2019-20. This report covers the City's revenue performance and expenditures incurred from July 1, 2019 through December 31, 2019 and identifies any major trends or variances in comparison to adopted budget levels. In addition, as budget assumptions and unanticipated changes arise during the year, Mid-Year Budget Adjustments amending the adopted budget are also presented for Council's consideration for approval.

RECOMMENDATION

1. Receive and file the second quarter financial report for FY 2019-20.
2. Approve the Mid-Year Budget Amendments

BUDGET POLICY PRIORITY STATEMENT

This item matches the following Budget Policy Priority Statement:

- Fiscal and Organizational Stability.

FISCAL IMPACT

The information provided in these reports will be used by Staff to ensure continued budgetary diligence over the remainder of the fiscal year and through the FY 2020-21 budget development process. The requested budget adjustments reflect amendments to

increase FY 2019-20 budgeted revenues in the amount of \$621,346 and appropriations to the operating budget (expenditures) in the amount of \$466,984. There is no significant net citywide fiscal impact, as requested revenues exceed requested expenditures.

DISCUSSION

Introduction

For FY 2019-20, the City of Fullerton continued to elect to adopt a one-year budget in order to concentrate on City Council priorities, organizational stability and efficiency, and stabilizing the financial future of the City. While the operating budget for all City funds (including Water, Sewer, and General Fund to name a few) for FY 2019-20 was structurally balanced, the City continues to experience and contend with several fiscal issues and challenges year in and year out. Some of these include: slow but steady revenue growth; rapidly increasing pension obligations due to continued lower than expected investment returns from CalPERS, the City's employees' retirement provider; employment retention and recruitment issues; and the need to support critical infrastructure capital improvement projects especially in our streets and roads. This has resulted in the City relying on the use of reserves, one-time revenues and vacancy savings to cover ongoing operating deficits.

City staff provides quarterly financial updates to the Council, which is a sound fiscal practice to report on the City's ongoing fiscal condition, to identify and correct any budget issues as they arise and is a tool to strengthen its financial planning efforts. The second quarter financial report provides a measurement of the City's overall fiscal health and condition relative to adopted budget levels. This report compares all revenues and expenditures from July 1, 2019 through December 31, 2019 in comparison to the budget. This report also covers adopted budget assumptions and City Council approved changes that have occurred since budget adoption. The projected budget does not include Mid-Year Budget Amendment requests as they are being presented to City Council for approval herein.

While assessing the fiscal condition of all City funds is important, the second quarter financial report will largely focus on the General Fund, as this is the City's chief operating fund that supports traditional municipal services, such as public safety, fire suppression, parks and recreation services and public works to name a few. All City funds are presented at a high level and specific funds will be discussed where needed.

All City Funds

All City Funds, as presented in Attachments 1 - 3, include all the City's Enterprise Funds, such as Water Utility and Sewer Enterprise, as well as all restricted funding (i.e. Gas Tax and SB1, etc.), all internal services funds, the General Fund and Capital Improvement Program (CIP). For all City Funds, actual revenues total \$92.7 million (42% of the amended revenue budget) and actual expenditures total \$83.8 million (42% of the amended expenditure budget) through December 31, 2019. Overall, total City Funds revenues and expenditures are within the expected range through the second quarter of the fiscal year. Capital Improvement Projects budget and their funding sources are

budgeted in whole for the fiscal year, but are not likely to be fully completed by the end of the fiscal year.

General Fund (including Library and Parks/Recreation)

The General Fund, as presented in Attachments 1 - 3, reflects actual revenues and expenditures recorded through December 31, 2019 and includes General Fund revenues of \$35.2 million (36% of the amended revenue budget) and General Fund expenditures that total \$47.0 million (48% of the amended expenditure budget). While this appears to show an ongoing deficit, this is very typical. Revenues are typically received in a non-linear fashion, in which the majority of the City's major revenues such as property taxes, sales taxes and franchise fees are received in the latter part of the year. Whereas the City is primarily a full-service city and personnel represents 70% of the budget, expenditures are more continuous as payroll is processed on a bi-weekly basis and certain equipment, supplies and contract expenditures/encumbrances are front loaded in the earlier part of the fiscal year.

Revenues

In total, General Fund revenues are up by 4.3% for FY 2019-20 in comparison to this same period last year when one time sale of property revenues are removed. This increase is largely due to the change in the ambulance billing contract by which the City records the gross revenue rather than the net "income" from ambulance services.

The City's major revenues, property tax and sales tax, continue to grow at a slow but steady pace and are both up 4.7% and 1.5%, respectively, from this point last year. Planning and Plan Check and Development Permits are also up from this point last year, which is a sign construction and development is occurring within the City.

Parking Revenues, including parking citations, are a new revenue source that is projected to bring in over \$200,000 annually. The City's new Downtown Paid Parking Program appears to be generating consistent revenues which are projected to offset the cost of enforcement and begin to support reinvestment in Downtown maintenance, safety and security.

Another revenue of particular interest is the City's ambulance revenues. FY 2019-20 is the first full year of recording ambulance revenues and total ambulance contract expenses in our books. The City has only received 42% of its budgeted revenues, however, this is due to receiving these rolling revenues one month in arrears. Staff is projecting these revenues will come in slightly above budgeted projections at \$4.0 million. Based on mid-year review, ambulance revenues are projected to cover the cost of these services (including adjustments for County mandated costs – see below) and yield the program net revenue as anticipated.

Overall, the General Fund is projected to end FY 2019-20 at \$100.0 million, \$2.3 million above the amended budget. This is largely due to higher than anticipated sales tax revenues (projected increase of \$1.2 million), which is due to new sales tax laws requiring marketplace (i.e. Wayfair or Etsy online websites) vendors and sellers to remit sales tax to local county pools and respective cities. This is also due to steady property tax growth

(projected increase of \$350,000), as well as one-time revenues of over \$600,000 as a result of a sale of City property (\$350,000) from the Successor Agency's Long Range Housing Property Management Plan and unanticipated revenue (\$250,000) resulting from an assignment change to the City's waste hauler agreement.

Expenditures

General Fund expenditures are tracking at the pace expected and are at 48% of the total General Fund budget through the midpoint of the fiscal year. General Fund expenditures are expected to come in on target with amended budget projections of \$98.1 million. While this is good news, it is important to note that the City's budget was balanced utilizing \$1.9 million of savings from existing position vacancies. Holding these positions vacant impacts retention and service levels and is not sustainable. The budget issues identified below are included in the City's Mid-Year Budget Amendments request.

Mid-Year Budget Amendments

Mid-Year Budget Amendments are required to ensure that budget and accounting records are accurately maintained as the fiscal year progresses. As changes in the organization occur and unanticipated issues arise, budget assumptions often need to be revisited and budget adjustments need to be made. The Mid-Year Budget Amendments for FY 2019-20 are shown in Attachment 4. In summary, when the City changed its ambulance services contract, there were unknown County mandated costs associated with ambulance services that the City is obligated to pay (~\$180,000) and is being requested for approval. During the first half of the fiscal year, City Council approved several department reorganizations, which added new positions, as well as reclassified several other positions many of which were cost neutral. However, some positions were not and the funding for these positions are now being requested. All other requested corrections to the budget are presented in more detail in Attachment 4. Mid-year budget expenditure requests total \$466,984 and will be offset by revenue adjustments totaling \$621,346.

Other Funds

The majority of the City's other major fund expenditures are tracking on pace and revenues are coming in as projected. The City's Water Utility and Sewer Enterprise funds are expected to come in at budgeted levels for both expenditures and revenues. Airport revenues are performing well and are up by 3.6% from last year's levels and have benefited from the updated hangar fees adopted earlier this fiscal year.

One fund of particular concern is the Brea Dam recreational fund. The primary activities in this fund include the Fullerton Golf Course and Tennis Center and other smaller programs, such as the Sports Complex. Last year, Golf Course (which subsidizes other Brea Dam activities) revenues came in below budgeted projections (by ~\$500,000), which was largely attributed to inclement weather conditions (and subsequent repairs to the golf course) and an overall general decline of golf play nationwide. For FY 2019-20, revenues are performing better than last year's levels to date (up by 2.7%) and are projected to come slightly under the adopted budget at \$2.8 million. Expenditures are also tracking on pace with budgeted projections and are projected to end the year slightly above \$2.8 million, resulting in a slight projected budget shortfall. Staff will continue to closely monitor

this fund and work to address any potential shortfall. Should projections come off target, the General Fund may be called upon to subsidize this fund at year-end.

Economic Outlook – Five Year General Fund Forecast

While the City has managed to control department spending and streamlined operations and delivery of vital services to our residents within our existing staffing structure, this is becoming increasingly challenging to sustain as staffing levels are extremely lean and financial resources are limited. This is further hindered by rising CalPERS pension costs, the need to support critical street and road projects, necessary upgrades to the City's Information Technology infrastructure, investments in the City's workforce, and resources to fund the City's homelessness initiative. In order to contend with these fiscal challenges, a Five Year General Fund Forecast is a sound financial planning tool which enables the City to assess its financial position in the fiscal years to come. As such, outlined below is the City's preliminary baseline Five Year General Fund Forecast.

	ADOPTED FY 19-20	PROJECTED* FY 20-21	PROJECTED FY 21-22	PROJECTED FY 22-23	PROJECTED FY 23-24
Beginning Fund Balance	\$22,481,174	\$24,557,846	\$22,779,364	\$17,883,845	\$13,507,145
Revenues					
Property Tax	45,258,000	46,163,160	46,163,160	47,086,423	48,028,152
Sales Tax	22,200,000	22,644,000	22,191,120	22,634,942	23,087,641
All Other Taxes & Franchises	10,640,970	10,853,789	10,874,782	11,092,277	11,314,123
Charges for Services	9,150,545	9,312,311	9,227,444	9,395,480	9,566,877
All Other Revenues	10,392,419	10,970,272	10,271,324	10,891,106	10,957,828
Total Revenues	\$97,641,934	\$99,943,532	\$98,727,829	\$101,100,229	\$102,954,621
Transfers In	300,000	300,000	300,000	300,000	300,000
Adjustments to Projected Revenues	2,349,103	-	-	-	-
Total Revenues & Transfers In	\$100,291,037	\$100,243,532	\$99,027,829	\$101,400,229	\$103,254,621
Expenditures					
Salary & Personnel Costs	49,845,246	49,870,535	50,002,948	50,155,767	50,342,778
CalPERS Pension Costs	19,244,935	22,961,216	24,290,419	25,248,669	25,496,825
Operations & Maintenance	28,551,753	29,190,264	29,629,981	30,372,493	30,835,854
Total Expenditures	\$97,641,934	\$102,022,014	\$103,923,348	\$105,776,929	\$106,675,457
Transfers Out	100,000	-	-	-	-
Adjustments to Projected Expenditures	472,431	-	-	-	-
Total Expenditures & Transfers Out	\$98,214,365	\$102,022,014	\$103,923,348	\$105,776,929	\$106,675,457
Operating Surplus / (Deficit)	\$2,076,672	(\$2,078,482)	(\$5,195,519)	(\$4,676,700)	(\$3,720,836)

The Five Year General Fund Forecast is developed utilizing a number of baseline

* Mild Recession projected in FY 20-21 with recession impacts incorporated into FY 21-22 projections.
incorporated into FY 2021-22 projections, in which revenues will either remain flat or

decrease. For all other years, the City projects a conservative 2% revenue recovery for all its revenues, including property taxes and sales taxes. On the expenditure side, there are no projected salary increases beyond any approved bargaining unit agreements. Operations and maintenance increases are in line with projected inflationary drivers.

Also it is important to note, the beginning FY 2019-20 General Fund balance of \$22.5 million is not all available to spend for any general purpose use. Of this amount, \$1.4 million is restricted; \$9.5 million is assigned for contingencies to comply with the City's minimum 10% reserve policy; and \$5.6 million is assigned for previously approved street and road capital infrastructure projects. Further, City Council has begun to allocate uses of the remaining \$5.4 million unassigned fund balance in FY 2019-20.

As illustrated above, the City's General Fund is projected to have an operating deficit in every subsequent year of the forecast with the fund balance projected to decrease from \$24.6 million to \$10.1 million (which represents a 59% decrease), well below the City's minimum 10% reserve target. The \$10.1 million includes amounts which are restricted and/or assigned for other uses which means that the assigned reserve amount (10% minimum policy) is less than the projected \$10.1 million. CalPERS pension costs continue to be the major escalator and will increase substantially by over \$6 million (33% increase) by FY 2023-24. Further, because the baseline forecast reflects operating deficits, the forecast does not include much needed annual General Fund increases to support the City's rapidly deteriorating streets and roads infrastructure nor does it address any new City initiatives, such as the City's homelessness initiative and necessary additional upgrades to its Information Technology infrastructure.

Ongoing Efforts

In FY 2019-20, the City is renewing agreements with all its bargaining unit groups. The City is committed to employing cost effective and cost sharing strategies to support the City's overall fiscal well-being, while also remaining committed to investments in the City's workforce. As agreements are ratified and approved, any resultant fiscal impacts to the City's overall financial position will be projected in the City's year-end estimates and updated financial forecasts.

In order to assist the City in meeting its projected pension obligations, the City established an IRS Section 115 Trust. The pension trust was set up to anticipate future year pension increases from CalPERS and City Council authorized initial funds be set aside to address these impacts.

In FY 2019-20, the City will undertake a full cost allocation plan financial study. A cost allocation plan will provide a defensible overhead and internal service fund allocation methodology. This financial plan will identify administrative overhead costs performed (i.e. performing invoice billing for the Water Fund) by central services staff in support of all City enterprise, special revenue and grant funds which supports cost recovery to the General Fund. The City intends to implement the cost allocation plan in FY 2021-22.

In FY 2019-20, the City implemented a new homelessness initiative to combat the homeless crisis within the City and larger county area. On July 2, 2019, the City Council authorized a pilot "Safe Parking" program as many homeless in Fullerton are currently living in their vehicles, which provides a sense of security for some. The Safe Parking

Pilot Program's primary goal is to provide families or individuals living in their vehicles who have strong ties to Fullerton, a safe and legal place to park, sleep at night, and ensure participant linkage and access to supportive services such as the Coordinated Entry System. The City is also working collaboratively with other agencies and is part of the North Orange County Service Planning Area (North SPA) and is funding part of the Placentia and Buena Park Navigation Centers. Additionally, the City has been working with the Illumination Foundation to open a 150 bed recuperative/navigation center within the City of Fullerton. The City is expected to receive restricted funding (SB2 funds) from the State to contribute to this regional cause and is anticipated to receive this funding by the end of the year.

The City's streets and roads and transportation infrastructure continue to be a critical need and major concern for the City. A large percentage (ranging from 30% - 45%) of its local and arterial streets are in poor or very poor conditions. Over the past two fiscal years, the City allocated combined one-time revenues totaling \$5.6 million towards its streets, but ongoing annual funding of at least \$6 million is required to maintain its streets at current conditions and much more is needed to improve them. Staff is looking at all avenues and options to continue supporting its streets infrastructure, which include use of continued transportation funding, identifying new grants and new revenue opportunities.

Next Steps

The FY 2020-21 Budget Adoption process is now underway. The Administrative Services Department will work closely and collaboratively with all departments to develop a budget that is in alignment with the City Council's policy priorities, ensuring we are fiscally conservative and responsible in our projections and budget plans and instilling fiscal accountability at every department level.

Further, efforts to continue to refine the Five-Year General Fund Forecast and develop a long-term 20-Year Financial Forecast are ongoing. The FY 2020-21 Preliminary Proposed Budget, Five-Year General Fund Forecast, and 20-Year Financial Forecast will be presented to City Council at a subsequent strategic budget study session to be held prior to adoption of the FY 2020-21 budget.

Attachments:

- Attachment 1 - Revenue Detail by Fund Report
- Attachment 2 - Expenditure Summary by Fund and Department Report
- Attachment 3 - Schedule of Changes to Fund Balances Report
- Attachment 4 - Proposed Budget Amendments