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Title: Fiscal Year 2020-2021 Mid-Year Budget Report and Update on Fiscal Year 2021-2022 Budget Development (Finance Director Charelian).
a) RECEIVE REPORT
b) APPROPRIATE FUNDS

Sponsors:

Indexes:

Code sections:

Attachments: 1. Fiscal Year 2020-2021 General Fund Summary, 2. Fiscal Year 2020-2021 All Funds Summary, 3. Budget Survey

Date	Ver.	Action By	Action	Result
2/16/2021	1	City Council Regular Meeting		

TO:
Honorable Mayor and Members of the City Council

THROUGH:
Bruce Moe, City Manager

FROM:
Steve S. Charelian, Finance Director
Libby Bretthauer, Senior Financial Analyst
Marcelo Serrano, Management Analyst

SUBJECT:
Fiscal Year 2020-2021 Mid-Year Budget Report and Update on Fiscal Year 2021-2022 Budget Development (Finance Director Charelian).
a) **RECEIVE REPORT**
b) **APPROPRIATE FUNDS**

RECOMMENDATION:
Staff recommends that the City Council receive the Mid-Year Budget Report for Fiscal Year 2020-2021 and Update on 2021-2022 budget development.

FISCAL IMPLICATIONS:
Current trends indicate the City's General Fund operating budget will finish Fiscal Year (FY) 2020-2021 with revenues exceeding expenditures by \$557,105. Expenditures are lower due to vacant staffing positions, and reduced costs for Contract-Professional Services and Materials-Supplies as a result of various operations modified or canceled due to COVID restrictions.

The FY 2020-2021 Adopted Budget included a General Fund transfer to the Proposition “A” Fund to alleviate a funding deficit for Dial-A-Ride and other transit programs. Once approved by the City Council, the City Funds Exchange Agreement with the City of Lancaster allows the City to expend \$188,125 in General Fund dollars in exchange for receiving \$268,750 in Proposition “A” dollars. Since this is no longer being handled as an interfund transfer, a General Fund expenditure appropriation of \$188,125 and a revenue adjustment of \$268,750 in the Proposition “A” Fund is necessary to complete the transaction.

Projected year-end transfers to other funds, including the Stormwater Fund, Street Lighting Fund, and Pension Stabilization Trust Fund, are expected to total approximately \$1.6 million.

Taking into account year-end projections and these anticipated transfers, the unreserved General Fund balance is projected to be \$3.7 million at fiscal year-end. Due to the anticipated amount of Capital Improvement Project (CIP) carryforwards, there will be no unreserved balance projected in the CIP Fund. Other Funds are trending as expected (Attachment).

BACKGROUND:

The City Council adopted the Fiscal Year 2020-2021 Budget on June 25, 2020, with a slight General Fund operating budget deficit of \$1,458.

Revenues	\$73,122,730
Expenditures	<u>73,124,188</u>
Adopted Surplus/(Deficit)	\$ (1,458)

To achieve this minimal deficit, the City Council adopted the Budget with several cost cutting measures made possible by years of prudent fiscal decisions that helped prepare the City for more challenging financial times. Temporary measures incorporated into the budget included the freezing of six vacant positions and reducing the charge-outs of Internal Service Funds, which are used to capture and allocate common costs across all departments. The reductions included a one-time decrease of \$400,000 in Information Technology Fund charges and the suspension of Fleet Rental and Fleet Maintenance Charges totaling \$2.1 million. Both of these funds had built a healthy fund balance over the last few years when actual expenditures came in lower than expected, consequently the funds were able to absorb the reduction in charge-outs.

A Budget Update for FY 2020-2021 was presented and discussed during the November 4, 2020, City Council meeting. At that time, the City Council approved additional General Fund appropriations of \$496,700 for COVID-related expenditures and made adjustments related to the cancellation of Special Events for \$293,600. In December, the City Council also appropriated \$250,000 for COVID-19 Small Business Loans. Taking into account all General Fund budget amendments to date, including encumbrances carried forward from the prior year, expenditures would exceed revenues by \$1,443,246 as budgeted. However, every January, City staff analyzes year-to-date activity and prepares mid-year projections for revenues and expenditures to evaluate potential budget variances and forecast year-end results. This report focuses on these mid-year projections and explains budget variances to provide a current depiction of the City’s fiscal position.

DISCUSSION:

The City Council and staff respond to the community’s needs in part through the budget. The budget is both a spending plan for the City’s available financial resources and the legal authority for the

City's various departments to spend these budgeted appropriations on goods and services that align with public priorities and meet the needs of Manhattan Beach residents.

In the current fiscal year, General Fund revenues are estimated to come in under the adjusted budget by \$1,485,825 (2.0%). Expenditures are projected to be \$3,486,176 (4.7%) under the adjusted budget (the adjusted budget includes City Council-approved amendments during the current year as well as encumbrances carried forward from the prior year).

When comparing estimated year-end revenues and expenditures irrespective of the budget, revenues are expected to exceed expenditures by \$557,105.

Adopted General Fund Surplus/(Deficit)	(\$ 1,458)
Net Budget Adjustments to date	(1,441,788)
Revenues under Budget	(1,485,825)
Operating Expenditures under Budget	<u>3,486,176</u>
Projected General Fund Surplus	\$ 557,105

General Fund Revenues

The following are highlights of several key revenue areas. Table 2 on the General Fund Summary Attachment summarizes key General Fund Revenues this fiscal year, including a comparison to prior year actuals. Historically, the three largest contributors to the City's General Fund revenue mix are Property Tax, Sales & Use Tax, and Transient Occupancy Tax.

Property Tax

Property Tax, which has been the strong foundation of the City's General Fund, now equates to about 50% of revenues. The City's Property Tax consultant, HdL, confirmed a 7.1% increase in net taxable assessed values for FY 2020-2021. This additional growth was due to new commercial parcels with added improvements, as well as residential and non-residential construction. With this higher than expected increase in assessed values, the Property Tax revenue category will total approximately \$36.2 million, which is \$1.1 million (3.0%) over the adopted budget and \$2.2 million (6.4%) over the prior year actual.

Real Estate Transfer Tax

Real Estate Transfer Tax revenue is derived from a charge of fifty-five cents per \$500 of sales price during the transfer of a property and is split evenly between the City and the County of Los Angeles. At the time the budget was adopted last June, there were valid concerns over the uncertainty of real estate sales occurring with virus concerns and Safer at Home orders. Due to these concerns, the budget for Real Estate Transfer Tax was conservatively estimated at \$650,000.

Per the latest available data for detached single-family home sales, Manhattan Beach had a higher transaction volume in 2020 with a total of 351 sales compared to 327 sales in 2019. About 70% of the sales recorded in 2020 occurred during the third and fourth quarters. The median price of a detached single-family residential home within the City increased to nearly \$2.6 million in 2020 (Source: HdL 2020-2021 Property Tax Data).

Based on transfer tax collections from all properties (residential and commercial) to date, revenues are expected to exceed the budget by \$150,000 (23.1%), yielding \$800,000 for the year.

Sales Tax

Sales Tax, the City's second largest General Fund revenue source (about 11.0% of total revenue), is projected to be \$42,778 (0.5%) over budget at \$8.2 million. Although trending better than the conservative budget amount, Sales Tax of \$8.2 million is \$207,953 or 2.5% below the prior year.

Operational restrictions at restaurants and brick-and-mortar retail locations are causing the lower trend. With in-person experiences limited, the shift toward online sales have increased the amount of taxes received through the State and County pools. However, the City share of those taxes are less than received from a physical transaction at a brick-and-mortar. Sales tax received from the State and County pools is forecasted to increase even more, corresponding with the final implementation of the Wayfair decision, wherein the Supreme Court decided that out-of-state retailers selling above certain thresholds into a State (e.g., California) can be required to collect and remit state sales & use taxes on their sales within the state.

As part of the response to the economic effects of the pandemic, Sales & Use Tax deferral programs were put into place at the State level. These programs extended the due dates for collections at large businesses and provided additional relief to qualified small businesses. Based on information collected by the City's Sales Tax Consultants (HdL), the City can expect to receive about \$600,000 in revenue from deferred payments and about \$301,500 from loan repayments in FY 2020-2021. The deferred payments and loan repayments are building into the year-end projections.

Transient Occupancy Tax

The travel and tourism industries have been one of the hardest hit by the COVID-19 pandemic, and Hotel Transient Occupancy Tax (TOT) collections illustrate the distress. TOT receipts were showing increases month-to-month, but area hotels expected a decrease in occupancy rates during the "offseason" winter months. The trajectory of COVID-19 trends in the spring will be critical for projecting TOT revenue in 2021 and beyond.

The City currently levies a 12% Transient Occupancy Tax (TOT) on hotel and motel rooms with the majority of the tax going to the General Fund. A small portion of the tax goes directly to the Capital Improvements Fund to fund debt service on the Police & Fire Facility and future projects. TOT revenues for the full year are expected to total approximately \$2.5 million, which is \$1.9 million (43.2%) below budget, and \$1.1 million (30.0%) below the prior year.

Business License Tax

Business license tax (BLT), which is generally calculated upon a business's prior year gross receipts, has remained level or had slight increases year over year, likely due to the fact that nearly 100 businesses (about 35%) pay the maximum gross receipts business license tax where changes in their gross receipts are unlikely to impact the total license tax paid.

However, the real impact of business closures in 2020 will be felt in the taxes coming due in 2021 because that tax due is based on 2020 gross receipts. Although the City Council has again extended the April 30, 2020 deadline to October 1, 2020 any revenues received within 60 days of the fiscal year end (June 30) will be calculated in FY 2020-2021. Considering the widespread closures and challenges that businesses faced in 2020, Business License Tax is now projected at \$3,175,000 which is \$150,000 (4.5%) below budget and \$477,228 (13.1%) below FY 2019-2020.

Plan Check and Building Permit Fees

On July 1, 2020, the City implemented a new fee schedule which, along with efficiencies in the

Energov software implemented in FY 2019-2020, has led to changes to the permitting and plan check processes. As a result, multiple permits were merged into one “combination” permit, making comparisons between this fiscal year and the previous year difficult. The volume of issued permits and plan checks have increased in the first half of FY 2020-2021, but the revenue received from both is lower compared to the same period during the previous fiscal year. There has also been a 38% drop in the number of demolition permits, pointing to a shift away from new construction, in favor of remodels. Notably, building record requests have increased, which coincides with the stable amount of home sales.

Taken together, Building Plan Check and Permit fees collected in FY 2020-2021 are anticipated to exceed budget by \$250,000 (8.4%) and be higher than the prior year by \$196,756 (6.5%).

Service Charges and Transfers

Revenue from other Service Charges (not including Plan Checks) is projected \$0.9 million (20.4%) under budget, mainly due to significant impacts to Parks and Recreation programs. Usually, summer programming generates a significant portion of Parks and Recreation revenues, but with operational changes required under the County health orders for activities and facilities still in effect, recreation programs will likely be impacted throughout 2021. As much as possible, staff created new “virtual” programs or modified existing classes and programs to comply with Los Angeles County Public Health Orders and affiliated approved modification guidelines. Due to the restrictions, the Parks & Recreation Department is offering about 60% fewer programs than last year. However, for programs eligible to open at reduced capacity, enrollments have been full.

Interest and Rents

The City invests its idle cash in a number of instruments, including the state-run Local Agency Investment Fund, corporate debt, U.S. Treasury notes and Governmental Agency securities. Interest rates are at historic lows for the foreseeable future as the current focus is steadying the economy after the pandemic. The portfolio was recently yielding 1.33% in December 2020, down from 2.15% one year prior. Interest income in the current fiscal year is now expected \$126,200 (13.6%) below budget at \$798,800.

Also in this category are rents and leases of City properties, including the rent paid by the Westdrift Hotel. Similar to Transient Occupancy taxes, this percentage rent is also lower due to occupancy rates not being at capacity.

From Other Governments

The From Other Governments category includes the CARES Act monies received to date (\$435,236) as well as various grants and reimbursements from anticipated from Federal, State and local agencies. The CARES Act, passed by the Federal Government on March 27, 2020, provided allocations to smaller cities through the State to assist in local governments’ response to the pandemic.

In addition, funding from the Federal Emergency Management Agency (FEMA) became available to various jurisdictions since the pandemic is classified as a State of Emergency. On January 21, 2021, the White House issued a memorandum to increase the FEMA reimbursements from 75% to 100% of eligible expenses. If approved, the City’s application, currently in the final review stage with FEMA, is eligible for up to \$813,599 of reimbursable expenditures through September 15, 2020.

Since FEMA released new guidelines that restricted reimbursable categories effective September 15,

staff anticipates that future reimbursement requests to FEMA will be significantly reduced compared to the previous submittals. While personal protective equipment (PPE), the cost of communication to the public, and coordinating vaccination efforts will be reimbursable under the new guidelines, the City will no longer be able to submit sworn overtime and legal fees. Staff will continue to monitor all opportunities for State and Federal level grants that may become available.

Other General Fund Revenues

In the Miscellaneous Revenue category is Workers' Compensation Salary Continuation, which is a reimbursement to the General Fund for wages paid to injured employees receiving benefits. Higher levels of this reimbursement revenue indicate increased workers' compensation claims activity. Based on activity through January 2021, reimbursement revenue is projected at \$500,000, which is below budget by \$200,000 or 28.6%.

Operating Service Transfers include the General Fund reimbursement per the Cost Allocation Plan adopted in February 2020 as well as Engineering staff time allocated to capital projects and grants.

General Fund Expenditures

Midway through the year, the City has expended or encumbered \$40.2 million (54.0%) of the total adjusted budget allocation. After a thorough review by all departments, General Fund expenditures are expected to end the year \$3.5 million (4.7%) under budget. Table 3 on the General Fund Summary Attachment breaks down General Fund Expenditures by category.

Salaries and Wages, which includes full-time, part-time, and overtime costs, is expected to be under budget at the end of the fiscal year by \$1.4 million (4.0%). Of this total, \$1.1 million in savings is attributed to a higher than expected number of unfilled full-time positions. Not included in this calculation are the six "frozen" vacancies (Cultural Arts Manager, Assistant Planner, Revenue Services Specialist, Older Adults Recreation Coordinator, and two Street Maintenance Worker I/II) that were excluded in the FY 2020-2021 Budget as a cost savings mechanism. All open positions, including those currently frozen, are being evaluated along with organizational needs for FY 2021-2022.

Part-time employee salaries are projected to be under budget by \$481,643 (22.9%) this fiscal year. Part-time employees are critical to the success of many City operations that are currently operating under-capacity or not at all due to COVID restrictions. The need for these part-time hours will re-emerge when these programs may be safely reinstated. However, as with full-time positions, part-time employee needs are also being assessed for efficiencies going forward.

Overtime costs are currently trending over budget by \$233,718 (4.9%), mainly due to Mutual Aid Overtime in the Fire Department. Reimbursement for these Mutual Aid engagements is included as a General Fund revenue within the Service Charges category.

Employee Benefits are estimated at \$454,305 (2.4%) under budget for the full year. Within this category, Group Medical Insurance is estimated under budget by \$303,267 (7.52%) due to position vacancies and some of the City's Group Medical Insurance plans experiencing lower premium increases than projected.

In addition to contributions for current year service, amortization payments on the City's unfunded pension liabilities are also included in the Employee Benefits category. In FY 2020-2021, the City's General Fund paid \$1.4 million for miscellaneous employees and \$3.8 million for Safety employees.

It should be noted that these payments are essentially “interest only” on the City’s unfunded liabilities and any significant reduction in the liability requires other measures such as the introduction of Pension Obligation Bonds. The City is currently in the process of issuing Pension Obligation Bonds (POBs) to refinance the City’s CalPERS liability debt, thereby replacing it with bond debt at much lower interest rates, to achieve significant budgetary savings over the next 22 years.

The Contract & Professional Services category includes consultant services, audit services, computer contract services, and legal services. The overall savings of \$718,523 (6.8%) in this category is due to budgeted contract services that will not be spent in the current fiscal year, primarily the result of projects and programs delayed and/or modified due to COVID restrictions. Most notable are the contracts for School Crossing Guards and various recreation program instructors that are not being utilized. At this time, these items have remained in the budget in order to be ready for when the programs return after the LA County Health Orders are lifted. Partially offsetting the savings within this category are Legal Services, which, based upon the first five months of the year, are projected to exceed budget by \$227,000 (24.2%) at year-end due to increased activity necessitated by addressing the COVID-19 pandemic, an upsurge in development projects (many of which have been appealed to the City Council), and the increase in lawsuits filed against the City. In turn, such additional expenses have been partially offset by keeping the Legal Secretary position vacant.

Materials & Services are expected to end the year under budget by \$518,130 (18.7%). As a result of most employees teleworking and recreation programs impacted by COVID restrictions, savings in Departmental Supplies, Office Supplies, and Printing costs are projected at \$324,304 (27.7%) below budget. Also in this category are Conferences and Training, which are expected to be under budget by \$225,802 (52.0%). Until travel and gatherings are safe, training will be attended virtually through webinars at greatly reduced costs.

Within this category are Bank Service Charges, which are currently trending \$103,995 (65%) over budget due to the fact that all payments for building permits and plan checks through the Energov Permitting system are now made online through a third-party portal. These Bank Services Charges are the cost of doing business electronically and recouped through the overhead charges included within the cost of the permits/plan checks.

Also within the Materials & Services category are one-time expenditures for COVID Business Loans (which will be repaid in future years with interest) and Proposition “A” City Funds Exchange. When the FY 2020-2021 Budget was adopted, a General Fund transfer to the Proposition “A” Fund was included to alleviate a funding deficit for Dial-A-Ride and other transit programs. The City Funds Exchange Agreement with the City of Lancaster allows the City to expend \$188,125 in General Fund dollars in exchange for receiving \$268,750 in Proposition “A” dollars. Since this is no longer being handled as an interfund transfer, a General Fund expenditure appropriation of \$188,125, and revenue adjustment of \$268,750 in the Proposition “A” Fund, is necessary to complete the transaction. This prudent use of General Fund dollars nets a savings of \$80,625 for the General Fund.

Utility costs are projected under budget by \$116,994 (12.1%). Cost increases assumed during budget development last year have not materialized, thus causing the lower trend in actual expenditures to date. Additionally, as employees continue to telework, ongoing savings are expected in telephone, electricity and water costs.

Internal Service Charges are expected to end the year nearly at budget. Fleet Rental and Fleet

Maintenance charges (totaling about \$2.1 million) were suspended in FY2020-2021 as a means to achieve temporary budgetary savings in the General Fund. Additionally, charges to the Information Technology Fund were reduced by \$400,000. Both of these funds had built a healthy fund balance and could absorb the reduction in revenue for one year. Staff is currently evaluating the City's Internal Service Funds (Insurance Reserve, Fleet, Information Technology, and Building Maintenance) for additional efficiencies and opportunities to maximize savings in FY 2021-2022.

Property and Equipment purchases are projected to come in under budget by \$310,534 (57.5%) due to one-time equipment and software purchases being carried forward to FY 2021-2022. Delayed projects and purchases include the completion of the Public Safety CAD/RMS Upgrade and technology enhancements for the Police Department facility, including a Bi-Directional Amplifier/Radio Signal Booster and Network Security upgrades.

Overall, General Fund expenditures are trending \$3.5 million (4.7%) under the adjusted budget.

General Fund Transfers to Other Funds

Over the next five years, General Fund subsidies to the Stormwater Fund, Street Lighting Fund, and Pension Stabilization Trust Fund are projected between \$1 million and \$2 million per fiscal year.

The Street Lighting & Landscaping Fund currently has no fund balance and assessments are inadequate to fund operations or provide for future capital needs. As a result, the General Fund subsidizes this fund every year, estimated at \$114,084 in FY 2020-2021.

The General Fund's subsidy to the Stormwater Fund is estimated at \$1,232,932 in FY 2020-2021. This Fund has been encountering higher operating costs due to legislative action to clean and limit stormwater runoff, which reduces funds for highly needed capital improvement projects. Some relief is provided by LA County Measure W, which is now providing an annual allocation of about \$410,000 to the City. In FY 2020-2021, the City expects to receive a total of \$820,000 for the current year allocation plus a catchup payment for the prior year. Stormwater assessments will remain unchanged until a Proposition 218 vote is passed, forcing the General Fund to continue supporting these ancillary services.

Lastly, the FY 2020-2021 General Fund Adopted Budget includes a transfer out to the Pension Rate Stabilization Trust Fund of \$250,000. The current balance of the Trust Fund is about \$1.76 million, including principal of \$1.5 million and accumulated interest. These funds are available to fund any pension-related payments to CalPERS at the City Council's discretion.

FY 2020-2021 MID-YEAR BUDGET SUMMARY

Development of the spending plan for FY 2020-2021 was mixed with uncertainty and concern about the severity and duration of the COVID-19 pandemic. Revenues were conservatively estimated and expenditures were reduced where possible while still maintaining current service levels. With just over half the year completed, General Fund revenues are mostly stable, although Sales Tax and Transient Occupancy Taxes are being closely monitored. Expenditure savings can be attributed to Salaries and Wages, Employee Benefits, and Contract and Professional Services. Irrespective of budget, revenues are expected to exceed expenditures at year-end.

Looking towards the future, the City is in the process of issuing Pension Obligation Bonds as a means to mitigate significantly rising pension costs. The savings generated by the debt refinancing may be used for future pension costs and/or used for capital projects. The City maintains a continual

focus on streamlining costs while preserving the levels of service provided to the community.

The projected General Fund surplus as well as the existing Unreserved General Fund balance provide an opportunity to allocate funds to City Council priorities, including capital projects. However, with about \$1.6 million in continuing transfers out to the Stormwater Fund, Street Lighting Fund and Pension Rate Stabilization Fund, the Unreserved General Fund balance is expected to decrease to \$3.7 million after FY 2020-2021. Funding essential operations and capital priorities will be discussed during the FY 2021-2022 budget process.

PUBLIC OUTREACH:

On Wednesday, February 3, 2021, the City launched a Budget Priorities survey. The survey, which received over 450 responses, was announced in an e-notification email and promoted on the City's social media accounts.

Future opportunities for public input include May 4, 2021, when the FY 2021-2022 Proposed Budget is presented to the City Council, and during subsequent City Council Budget Study Session(s). Questions and comments may also be submitted to Budget@citymb.info.

ENVIRONMENTAL REVIEW:

The City has reviewed the proposed activity for compliance with the California Environmental Quality Act (CEQA) and has determined that there is no possibility that the activity may have a significant effect on the environment; therefore, pursuant to Section 15061(b)(3) of the State CEQA Guidelines the activity is not subject to CEQA. Thus, no environmental review is necessary.

LEGAL REVIEW:

The City Attorney has reviewed this report and determined that no additional legal analysis is necessary.

ATTACHMENTS:

1. Fiscal Year 2020-2021 General Fund Summary
2. Fiscal Year 2020-2021 All Funds Summary
3. Budget Survey