



Legislation Text

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TO:

Honorable Mayor and Members of the City Council

THROUGH:

Bruce Moe, City Manager

FROM:

Steve S. Charelian, Finance Director

Henry Mitzner, City Controller

Libby Bretthauer, Financial Analyst

SUBJECT:

Receive the Fiscal Year 2018-2019 Mid-Year Budget Report and Update on Fiscal Year 2019-2020 Budget Development (Finance Director Charelian).

- a) **RECEIVE MID-YEAR BUDGET REPORT FOR FISCAL YEAR 2018-2019**
- b) **RECEIVE UPDATE ON BUDGET DEVELOPMENT FOR FISCAL YEAR 2019-2020**

RECOMMENDATION:

Staff recommends the City Council:

- a) Receive the Mid-Year Budget Report for Fiscal Year 2018-2019; and
- b) Receive an update on budget development for Fiscal Year 2019-2020.

FISCAL IMPLICATIONS:

Current trends indicate the City's General Fund operating budget will finish Fiscal Year (FY) 2018-2019 with revenues exceeding expenditures by approximately \$2.5 million. Expenditures were lower largely due to vacant staffing positions in various stages of recruitment. Projected year-end transfers to other funds, including the Stormwater Fund, Street Lighting Fund, and Pension Stabilization Trust Fund, total approximately \$1.6 million. In addition, the adopted budget includes transfers out to the CIP Fund (\$547,600) and IT Fund (\$600,299) for one-time projects. Taking into account year-end projections and these anticipated transfers, the unreserved General Fund balance is projected to be \$5.5 million at fiscal year-end. Other Funds are trending as expected.

BACKGROUND:

The adopted budget represents the organization's spending plan, which takes into account all available resources that may be utilized to fund and achieve the City's priorities for the fiscal year. The Fiscal Year 2018-19 Budget was adopted on June 19, 2018, with a General Fund operating budget deficit of \$184,754.

Revenues	\$75,505,117
Expenditures	<u>75,689,871</u>
Adopted Surplus/(Deficit)	(\$184,754)

Although ongoing operations are fully funded by ongoing revenues, one-time expenditures such as the digital interoperability radios and MBUSD safety and security enhancements were budgeted, which resulted in the deficit. Any expenditures exceeding revenues at year-end would have been spent from the Unreserved General Fund balance.

DISCUSSION:

Overall, the FY 2018-2019 General Fund budget-to-actuals through mid-year are performing better than expected. Revenues are estimated to exceed the adjusted budget by \$619,289 (0.8%). Expenditures (including all budget adjustments subsequent to adoption) are expected to total \$3,079,648 (4.0%) 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 \$2,528,669.

Adopted General Fund Surplus/(Deficit)	(\$184,754)
Net Budget Adjustments to date	(985,514)
Revenues exceeding Budget	619,289
Operating Expenditures under Budget	3,079,648
Projected General Fund Surplus	\$2,528,669

General Fund revenues are generally stable, with limited growth potential after several years of post-recession increases. Savings are predicted in several expenditure categories due to position vacancies and other savings realized through cost controls.

General Fund Revenues

The following are highlights of several key revenue areas. Please see Table 2 on Attachment #1 for General Fund Revenues, including a comparison to prior year actuals.

Property Tax

Property tax is the General Fund's largest revenue source, accounting for approximately 42% of total revenue. At nearly \$32.0 million, Property Tax as a category is anticipated to come in \$302,526 (1.0%) over budget and \$1,641,889 (5.4%) ahead of last year. Net taxable assessed values have grown 6.2% from fiscal year 2018, reflecting the continued strength of the Manhattan Beach housing market. In the prior year, net taxable assessed property values grew by 7.0%.

Real Estate Transfer Tax

Real Estate Transfer Tax revenue is derived from a charge of fifty-five cents per \$500 of sales price, split evenly between the City and the County of Los Angeles. Per the latest available data for detached single-family home sales, Manhattan Beach has maintained steady, but lower, volume in 2018. However, median prices have continued to grow and even exceeded \$2.5 million in the fourth quarter of 2018. In 2018, detached Single Family Residential Home Sales totaled 329, at a median price of \$2,400,000. In the prior calendar year, sales volume totaled 383, with the median price of sales at \$2,360,000. (Source: HdL 2018-2019 Property Tax Data).

Based on transfer tax collections from all properties (residential and commercial), collections are

expected remain at budget (\$750,000).

Sales Tax

Sales Tax, the City's second largest General Fund revenue source (11.9% of total revenue), is expected to remain flat at around \$9.1 million. Modest growth projections made in consultation with the City's sales tax consultants indicate Sales Tax for the current year should come in above the prior year but slightly less than the budgeted projection. Continued increases in on-line sales/declining retail "Point of Sale" returns and relatively low fuel prices have contributed to the sluggish growth.

Transient Occupancy Tax

Also known as the hotel bed tax, the City currently levies a 10% Transient Occupancy Tax (TOT) on hotel and motel rooms with 8.5% going to the General Fund. The remaining 1.5% goes directly to the Capital Improvements Fund to fund debt service on the Police & Fire Facility and future projects. This year, TOT revenues have been negatively impacted by remodeling activity at the Residence Inn during the first half of the fiscal year. TOT revenues for the full year are expected to total \$4.5 million, which is \$25,000 (0.6%) above budget, and \$760,316 (20.2%) above the prior year, which was significantly impacted by the remodel of the Westdrift (formerly Marriott) Hotel.

Plan Check and Building Permit Fees

Taken together, Building Plan Check and Permit fees collected in FY 2018-2019 are anticipated to remain at budget, but will be lower than the prior year by \$235,245 (6.0%).

Plan check fee revenues are expected to come in at budget (\$1.8 million). In the first six months of the fiscal year, both the volume of plan checks and total valuation is lower than the same period one year ago.

As with plan checks, building permit fee revenues are expected to come in at budget at nearly \$1.9 million. Although the number of building permits issued in the first six months of the fiscal year was lower than the prior year, the total valuation of issued permits was significantly higher due to larger-scale developments, including the Manhattan Village Mall.

Business License Tax

Business license tax, which is generally calculated upon a business's gross receipts, has remained level or had slight increases year over year, likely due to the fact that around 80 businesses pay the maximum gross receipts business license tax, and changes in their gross receipts are unlikely to impact their total license tax paid. Total business license tax in FY 2018-19 is expected to reach nearly \$3.9 million.

Interest Income

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. During the last recession and associated economic problems, interest rates declined dramatically and remained at very low levels for several years. The Federal Reserve's recent benchmark interest rate increases have improved yields, resulting in the City's maturing investments to be reinvested at marginally higher rates. The portfolio was recently yielding 2.150% in January 2019, up from 1.615% one year prior. Global economic and financial developments, as well as muted inflation pressures,

have weakened the case for additional rate increases in 2019. Interest income in the current fiscal year is therefore expected to remain near budget at \$880,099.

Other General Fund Revenues

Worth noting 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, with higher levels indicating increased workers' compensation claim activity. Based on recent workers' compensation claim activity in FY 2018-2019, reimbursement revenue is projected to come in significantly above budget at \$1.1 million.

General Fund Expenditures

Midway through the year, the City has expended or encumbered \$40.9 million (53.3%) of the total adjusted budget allocation. After a thorough review by all departments, General Fund expenditures are expected to end the year \$3.1 million (4.0%) under budget. Table 3 on Attachment #1 breaks down General Fund Expenditures by category.

Salaries and Wages overall are expected to be under budget at the end of the fiscal year by \$1.3 million (3.9%). Within this category, regular salaries are projected to be under budget by \$991,413 (7.3%) due to open positions. The City has filled all key non-sworn positions, most recently the Human Resources Director. Other open positions are in various stages of the recruitment process, including Fire Chief, Public Works Inspector, Electrician, Traffic Engineering Technician I/II, Engineering Technician I/II, Community Services Officer, Account Services Representative, Administrative Clerk, Human Resources Manager and Revenue Services Manager.

Part-time salaries overall are estimated to end the year over budget by \$38,658 (1.7%). Significant variances to note include Parks and Recreation Administration and the Older Adults Program. In Administration, an experienced part-time employee with expertise in branding and design was temporarily added to help with the City's branding initiative. This work is nearing completion and will be finalized in March.

Demand for the Older Adults Program has increased after the Senior Advisory Committee set goals to actively market existing programs and develop new programs to meet the needs of the older adult community. As a result, there has been an increase in participation, programs and interest in developing even more new programs. Part-time staffing needs have increased to maintain an appropriate staff-to-participant ratio to ensure safety. Additionally, more weekend and evening programs have been developed like *Coffee, Technology and You* and a *Caregiver Support* group, which require staff on duty.

Sworn salaries (Police and Fire) are trending \$696,820 (5.3%) under budget for the full year also due to vacancies. A majority of the savings is derived from openings for the Fire Chief as well as two Police Sergeant positions. Police Department Sworn Overtime is projected to end the year \$81,953 (5.2%) under budget despite its current use in backfilling multiple open positions to maintain current service levels. Fire Department overtime costs are currently trending \$72,732 (3.9%) over budget due to the required backfilling of positions for employees currently on injury leave.

Employee Benefits are estimated at \$929,253 (5.5%) under budget for the full year. Within this

category, Group Medical Insurance is estimated under budget by \$449,471 (10.8%) due to position vacancies and some of the City's Group Medical Insurance plans experiencing lower premium increases than projected.

The balance of the savings in Employee Benefits is predominantly due to the City's employer pension contributions. Due to the aforementioned position vacancies, employer pension contributions for current year employee service are expected to be under budget for both regular employees and sworn employees by \$184,795 (14.8%) and \$176,830 (7.1%), respectively. Although there is a direct relation between pension contributions and salaries, the savings in these categories will not correlate exactly since: 1) exiting employees may "cash out" accumulated leave balances, and 2) overtime wages are not "pensionable" wages.

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 2018-2019, the City's General Fund paid \$1.0 million for miscellaneous employees and \$2.6 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 would require additional discretionary payments. Staff is currently developing recommendations for a long-term funding plan.

Contract & Professional Services includes consultant services, election costs, computer contract services, and legal services. The overall savings of \$432,151 (6.3%) in this category is the result of budgeted items that will not be spent in the current fiscal year.

Materials & Services are expected to end the year under budget by \$131,325 (2.9%), and Utility costs are projected under budget by \$120,408 (10.4%). In both of these categories, cost increases assumed during budget development last year have not materialized, thus causing the lower trend in actual expenditures to date.

Internal Service Charges are slightly over budget, mostly due to a 12.3% spike in Fleet Maintenance expenditures attributed to the cost of necessary repairs and safety enhancements on ambulances and police vehicles.

Property and Equipment purchases will exceed the budget by roughly \$68,218 (4.2%), mainly due to peripheral radio equipment needs that were not included in the budgeted cost for the new digital Motorola radios. Sufficient funds were available to cover the full cost of the new radio equipment that was purchased for the Police and Fire departments as well as Public Works and Code Enforcement staff who work in the field. During an emergency, this communications equipment will be critical for City staff to communicate locally as well as regionally with other jurisdictions.

Overall, General Fund expenditures are trending \$3,079,647 (4.0%) under budget.

General Fund Transfers to Other Funds

All other City fund revenues and expenditures have also been reviewed. Halfway through the fiscal year, other funds are trending at appropriate levels given historical spending trends and identified spending patterns.

Worth noting are other funds receiving subsidies from the General Fund, which diverts resources

from public safety and other general governmental services. Over the next five years, General Fund subsidies to the Street Lighting & Landscape District Fund and Stormwater 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 \$179,962 in FY 2018-2019.

The General Fund's subsidy to the Stormwater Fund is budgeted at \$1,248,046 in FY 2018-2019. This fund is encountering higher operating costs due to legislative action to clean storm water runoff and limits, which reduces funds for highly needed capital improvement projects. While these issues require a Proposition 218 vote, it is most appropriate that the General Fund no longer support these ancillary services.

In addition to these annual transfers, the City Council approved a phased transfer plan from the General Fund Unreserved Fund Balance to the Insurance Fund on November 17, 2015 to correct a fund imbalance that was a result of higher than expected claims activity during FY 2014-2015. Transfers in the amount of \$667,000 occurred in fiscal years 2015-2016, 2016-2017 and 2017-2018. Due to increased activity in liability claims, year-end expenditure estimates total \$6.6 million, which is \$145,646 above budget but \$714,030 less than the prior year actual. Staff has been monitoring these trends and is developing recommendations to adequately address these increasing costs for the long-term. If expenditures exceed budget staff will prepare a report to City Council for appropriation of additional funds.

Lastly, the FY 2018-2019 General Fund Adopted Budget included two one-time transfers out for specific projects budgeted in other funds. To fund the Enterprise Resource Planning (ERP) software system in the Information Technology Fund, a one-time transfer of \$600,299 was needed from the General Fund. The City Council also approved a one-time transfer to the CIP Fund in the amount of \$547,600 to pay for design work of Fire Station #2.

FY 2018-19 MID-YEAR BUDGET SUMMARY

Overall, Mid-Year results are trending as expected. General Fund revenues are stable and reflective of the local economy. Revenues are expected to outpace budget by \$619,289 while expenditures are expected to come in \$3,079,648 under budget. This can be attributed to the increases in Property Tax as well as savings in Salaries and Wages and Employee Benefits. Irrespective of budget, revenues are expected to exceed expenditures at year-end. Although the timing of the next recession is unknown, the City is preparing for more challenging times with minimal growth in revenues compounded by significantly rising pension costs. Therefore, a continual focus is streamlining costs while maintaining the levels of service provided to the community.

BUDGET DEVELOPMENT FOR FY 2019-2020

As requested by the City Council during last year's budget adoption hearing on June 19, 2018, Attachment #2 identifies potential budgetary savings from the FY 2019-2020 Approved Budget. These items, as identified by staff, are sorted by the anticipated level of impact on the Community and organization. Staff recommends the City Council review these items and provide direction on whether to incorporate any of these reductions in the FY 2019-20 Proposed Budget that will presented during the May 7, 2019, City Council meeting.

PUBLIC OUTREACH/INTEREST:

Future opportunities to provide input on the FY 2019-2020 Budget include May 7th, when the Proposed Budget is presented to the City Council, and subsequent City Council Budget Study Session(s). Tentative dates being held for one or more Budget Study Sessions include May 14, 16, and 23. The public hearing and formal budget adoption will occur in June.

Questions and Comments may also be submitted to Budget@citymb.info [<mailto:Budget@citymb.info>](mailto: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 2018-2019 General Fund Summary
2. Fiscal Year 2019-2020 Budget Cuts by Department