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Staff Report for Presentation on Preliminary Fiscal Year FY 2021-22 and 2022-23 Budget

### SUMMARY AND RECOMMENDATIONS

Presentation on the Preliminary Fiscal Year FY 2021-22 and 2022-23 Budget.

### BACKGROUND

The City Council approved the last biennial budget for the Fiscal Year (FY) 2019-20 and 2020-21 General Fund and other funds on June 3, 2019. Approved budgets are the annual expenditure plan and resource allocation guiding and ensuring implementation of City Council policies and priorities. The budget implements the vision, values, and direction for the broad range of services meeting the needs of the community in accordance with City Council policy.

Staff is presenting the preliminary budget to frame the budget development and update the City Council on the upcoming two-year budget for FY 2021-22 and 2022-23. The purpose of the preliminary budget is to project revenues supporting City services and comparing revenues to the current costs for maintaining existing services. The preliminary budget assumes continuation of current staffing levels, professional services, supplies, maintenance, and utilities. The focus of the preliminary budget is the General Fund since it comprises the unrestricted and therefore most flexible funds of the City supporting program objectives.

The Budget Task Force recommendations, Unfunded Capital Improvement Projects, Federal American Rescue Plan funding, and the use of Reserves are not included in this base-line budget. Part of the discussion on April 26, 2021 will include these topics.

### INTRODUCTION

The multi-year forecast for key operating funds is a critical budgetary tool providing a multi-year view

of revenues and expenditures. This tool helps the City Council evaluate impacts of policy choices on the long-term fiscal health of the City. The forecasting model enables the City Council to act more strategically by better understanding the future impact of current decisions.

A variety of assumptions and factors drive the forecast, such as labor costs, inflation, potential recession, federal and state regulatory requirements, statewide initiatives, short-term tax shortfalls, and unforeseen emergencies. These assumptions impact revenue and expenditure projections and variations can cause wide swings in budget balancing strategies. At the April 26, 2021 meeting, staff will present the General Fund preliminary long-term forecast to the City Council and provide insight into future financial capacity.

### CITY COUNCIL GOALS

The following City Council goals serve as a guide for upcoming budgets and provide overall direction for City services and programs. These goals were reaffirmed by the City Council at the Annual Planning Session on February 6, 2021.

- Place San Leandro on a firm foundation for long-term sustainability.
- Advance projects and programs promoting sustainable economic development, including transforming San Leandro into a center of innovation.
- Provide quality public safety service and grow our partnership with the community to keep San Leandro safe.
- Maintain and enhance San Leandro's infrastructure.
- Support and implement programs, activities and strengthen communication that enhances the quality of life and wellness, celebrates the arts and diversity, and promotes civic pride.
- Maintain and support a strong positive relationship between the City, schools, and the educational community.
- Promote and maintain an inclusive work environment that values employees and volunteer contributions, supports professional growth and development, and fosters a culture of kindness and collaboration in the delivery of services to our community.

### PRELIMINARY GENERAL FUND SUMMARY

The General Fund is the general operating fund for the City and accounts for all unrestricted financial resources except those required to be accounted for in another fund. Attachment 1 provides the Preliminary General Fund Summary for FY 2021-22 and 2022-23. The General Fund finances the operations of all basic municipal services. The preliminary FY 2021-22 budget projects revenues totaling \$121,883,000 and expenditures totaling \$121,820,000; the preliminary FY 2022-23 budget projects revenues totaling \$127,358,000 and expenditures totaling \$128,107,000. The projected revenue/expenditure balance is \$63,000 in FY 2021-22, with a projected deficit of \$749,000 in 2022-23.

As part of the budget development, City departments submitted budget proposals for consideration. The City Manager's Office and the Finance Department are currently evaluating the proposals and the requests are not included in the preliminary budget. The anticipated federal stimulus funds are also not included in the preliminary budget and will be incorporated into the final budget pending guidelines from by the U.S. Treasury. Please note that staff continues to refine the revenue and expenditure projections based on updated financial data. After receiving feedback from the City Council and the community on April 26, 2021, the budget will be further modified to reflect City Council direction. Staff is planning to present the Proposed Budget to the City Council in May 2021 along with further budget balancing strategies.

### HIGHLIGHTS OF MAJOR TAX REVENUE SOURCES

- **Property Tax** - Total property-related tax revenues increased by \$793,000 in the preliminary budget compared to the 2020-21 amended budget. Secured Tax and Redevelopment Residual Property Tax revenues make up 62% of the City's annual Property Tax revenue. Preliminary Secured Tax revenue amounts to \$14,093,000 in FY 2021-22 while Redevelopment Residual Tax amounts to \$2,584,000. Property Tax is the City's second largest revenue source and represents about 22% of total General Fund revenue.
- **Sales/Transaction Taxes** - The Sales/Transaction Tax revenues increased by \$4,203,000 compared to the 2020-21 amended budget. The budget for 2020-21 reflected adverse impacts from COVID-19 affecting taxable transactions. The original budget of \$38,986,000 was later increased to \$44,438,000 following the mid-year

budget review. Avenue Insights, the City's sales tax advisor, projects the City will receive \$48,641,000 in FY 2021-22. This favorable report on the recovery in taxable transactions is critical as Sales and Transaction Taxes are the City's largest revenue sources and make up 40% of the General Fund revenue.

- **Utility Users Tax (UUT)** - Total UUT revenues increased slightly by \$330,000 in the preliminary budget compared to the 2020-21 amended budget. The FY 2021-22 budget is projected at \$10,672,000. Natural gas and electric UUT revenues represent about 73% of the total UUT revenues. UUT is not expected to increase significantly in future years due to the use of renewal energy and increased competition in the telecommunication market (e.g., cable TV and wired and wireless telecommunications).
- **Real Property Transfer Tax (RPTT)** - The Property Transfer Tax revenues increased by \$2,000,000 compared to the 2020-21 budget. Ballot Measure VV was approved by city voters in November 2020. The measure authorizes increasing the Transfer tax rate from \$6 per \$1,000 in valuation to \$11. The amended 2020-21 budget was increased by \$3,200,000 at mid-year and the preliminary budget proposes an additional increase of \$2,000,000 in the first full year of Measure VV funding. RPTT revenues are projected at the \$9,000,000 level.
- **Business Licenses Tax** - The Business License Tax revenues decreased by \$570,000 compared to the 2020-21 budget. The budget decrease to revenue of \$5,830,000 primarily arises from the closing of one of the parking operator business as a result of the Pandemic (primarily serving long-term parking at the Oakland International Airport). The business was the significant taxpayer in the parking lot classification arising from Measure OO.

### ECONOMIC GROWTH AND INFLATION

Change in the Consumer Price Index is an important factor, directly impacting City revenues and expenditures. Inflation-sensitive revenues, such as sales and business license taxes, make up a significant portion of the General Fund budget (45%). The change in CPI for the San Francisco Bay Area increased by 1.6% in the past 12-months.

Changes in funding for most revenue categories include adjustments consistent with the rate of inflation. The established growth index for the 9-1-1 Emergency Communication Access Tax, Emergency Medical Services Tax, and the Business License Tax is CPI change of 1.6% for FY 2021-22. The new tax rates and the updated master fee schedule will be presented to the City Council for approval in May 2021.

### PERSONNEL AND STAFFING COSTS

As a service organization, the City's primary costs are related to labor, or roughly half of the General Fund budget. General Fund salaries and benefits are projected at \$58,618,000 for FY 2021-22. Projected FY 2021-22 staffing costs are expected to be significantly higher than the 2020-21 amended budget. Impacted by the COVID-19 pandemic, certain full-time and part-time positions were not filled, resulting in additional vacancy savings. These one-time savings are not expected to continue and are therefore no included in the preliminary budget. Key expenditures and assumptions are described below.

#### Salary Adjustments

The preliminary budget forecasts salary adjustments based on existing labor for all labor groups. Salaries and benefits for periods in FY 2021-22 and 2022-23 outside existing Memorandums of Understanding (MOUs) are adjusted by 2%.

#### Medical Insurance

Medical and dental insurance costs include estimated increases. The preliminary budget and the multi-year forecast include annual 4% rate increases.

#### Retirement Plan Costs (CalPERS)

The City contracts with CalPERS to administer its pension plans. Pension costs are made up of two parts including normal cost and unfunded liability amortization. Normal cost represents service credits earned by active employees in the current year and is calculated as a percentage of payroll. Based on the 2019 actuarial valuation reports provided by CalPERS, the normal cost rates for Miscellaneous and Safety plans are expected to remain close to the 2020-21 rates. While benefits remain unchanged, pension contributions are expected to increase due to prior year CalPERS portfolio losses and changes in actuarial assumptions. Pension costs are projected to increase by 9% in FY 2021-22 estimating at approximately \$21,500,000 for all funds. Please note that the unfunded pension liability includes costs for firefighters who

separated from the City when fire services were contracted out to Alameda County.

As noted below, over the years the City has taken proactive steps to buy down its unfunded liabilities. The Finance Committee has been evaluating funding strategies for pension liabilities, including the creation of a Pension Trust. The City's Other Post-Employment Benefits (OPEB) liability is adequately funded.

#### Unfunded Liabilities

Unfunded liabilities fall into two main categories: pensions and OPEB. Pension liabilities refer to the City's employee retirement plan with CalPERS. For an extended period, CalPERS investments performed above expectations and cities' retirement plan contributions were unremarkable. More recently and especially since the Great Recession, CalPERS returns have under-performed.

Lower returns, and several years of real losses, have resulted in significant annual contribution cost increases to cities (even for lower retiree benefits). In addition, CalPERS revised its assumptions measuring life expectancies, rates of return on investments, and the pay-back period for unfunded liabilities. These actions led to a steep increase in City costs to CalPERS.

OPEB refers to health benefits for employees having retired from City service. The City maintains a retiree health care plan that is relatively modest in scope but has long-term financial liability associated with the benefit.

The City has implemented a number of measures to reduce its unfunded liabilities including offering less generous benefit formulas, pre-funding unfunded pension contributions, requiring employees to pay the full employee share of their benefits and cost share from Safety employees. The Council also established the PULL (Prioritization Unfunded Liability Liquidation) Plan to fund pension and OPEB liabilities. Today the OPEB plan has reached a healthy funded status of 81%.

It is important for the City to continue to fund its obligations. Funding unfunded liabilities helps the City to stabilize costs and sustain services and programs in the long run.

#### Fire Contract

The FY 2021-22 preliminary budget for the fire services contract with the Alameda County Fire Department amounts to \$26,009,000 and this amount is expected to increase to \$26,969,000 in FY 2022-23. Estimated year-end savings are included in the preliminary budget resulting in the slightly lower amounts. The contract is for providing both emergency and non-emergency fire services in San Leandro. The FY 2020-21 amended budget for contract services amounts to \$25,578,000 before estimated savings.

### **OTHER BUDGET IMPACTS**

#### Debt Service Payments

Debt Service payments are based upon established debt payment schedules for General Fund debt and loans, Special Assessment Funds Debt, Water Pollution Control Plant debt, Successor Agency debt, Shoreline Enterprise Fund debt, and San Leandro Public Financing Authority debt. These debt payment schedules were used for the forecast projections of debt service in subsequent years. General Fund debt service payments are close to \$6,500,000 for each budget year.

### **PROPOSED PERSONNEL AND SERVICE ENHANCEMENTS**

The preliminary budgets for 2021-23 contain limited personnel enhancements and changes. Staffing modifications since adoption of the 2019-20 and 2020-21 biennial budget include:

- Administrative Assistant III (position added in City Clerk Office related to public record requests)
- Police Lieutenant position (eliminated in Police relocation)
- Police Sergeant position (eliminated in Police relocation)
- Police Officer position (eliminated in Police relocation)

One new full-time temporary position is proposed in preliminary budget, which will be offset by direct fees, existing

vacancies and the underfilling of an existing authorized position.

- Project Specialist II (Planner II) position in the Community Development Department

### **AMERICAN RESCUE PLAN ACT**

On March 11, 2021, the American Rescue Plan Act was signed into law. The Rescue Plan expands existing COVID-19 relief programs and provides additional funding to states and local governments that had not been included in the prior relief packages.

Counties and cities with population over 50,000 will receive funding directly from the Federal government. A total of \$350 billion has been directly allocated to states, counties, tribes, and territories, with a broad definition of allowable uses, and added purposes like recoupment of lost revenue and investments in water, sewer, and broadband infrastructure. While governments have flexibility in using these funds, they cannot use them to pay for pension costs or to offset or delay a tax increase. These funds must be used by December 31, 2024.

The City is awaiting the anticipated regulations regarding the use of funds. Staff will return to the City Council to propose projects and associated budget adjustments when those guidelines are published.

### **COMMUNITY ADVISORY BUDGET TASK FORCE**

The City Council created the Community Advisory Budget Task Force to seek budgetary and fiscal input from a select group of citizens. The Task Force was to report on community priorities, budget strategies related to revenues and expenditures, and the re-allocation of funds from the Police Department budget.

The City Council received the recommendations, offered feedback, and gave staff direction to review the recommendations. Staff will work internally to review the recommendations and assess those current in progress, ones requiring funding, the timing of possible implementation, and the internal capacity to accomplish the recommendations. An update will be provided to the City Council on April 26, 2021.

The City Manager's Proposed Biennial Budget for FY 2021-22 and 2022-23 will be presented to the City Council in May 2021. A public hearing and the adoption of the budget is scheduled for June 2021.

### **ATTACHMENT**

- Preliminary General Fund Summary

### **PREPARED BY**

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