



# City of Emeryville

CALIFORNIA

## MEMORANDUM

**DATE:** September 1, 2017

**TO:** Carolyn Lehr, City Manager

**FROM:** Susan Hsieh, Finance Director

**SUBJECT:** **Presentation and Review of the City of Emeryville Proposed Budget for Fiscal Years 2017-2018 and 2018-19**

### RECOMMENDATION

Staff recommends that the City Council review and discuss the Proposed Budget for Fiscal Years 2017-18 and 2018-19

### BACKGROUND

The City operates on biennial budget cycles, and the two-year budget format provides a longer-term look at the City's financial condition. The proposed budget allocates resources in accordance with the City Council's policy goals.

The proposed budget is premised on the long-term budget philosophy of the City Council and includes the following major principles:

- 1. Current year expenditures should be supported by current year revenues. One-time revenues should not be used for ongoing costs, but should instead be used for necessary one-time expenditures or to strengthen fund reserves.*
- 2. Fund balances should be maintained in all major operating funds that provide for unforeseen circumstances. The appropriate level of fund balance depends on the particular fund.*
- 3. Unfunded liabilities should be identified and funded with surplus funds when they are available. Liabilities that are currently accruing should be funded currently.*
- 4. When necessary, a strategy should be formulated and implemented to address potential impacts of the State budget and other State actions that may affect City revenues.*
- 5. The operating costs of any planned capital improvement should be estimated in the planning stage, so that these amounts can be recognized and budgeted.*

The 2017-19 budget is a balanced plan without drawing into General Fund reserves.

This was accomplished by budgeting certain General Fund contributions/expenditures in fiscal year 2017-18 instead of 2018-19 as Year 2 needed additional resources to support expenditures. The City is contemplating bond measures as part of the revenue study. If the City decides to issue bonds in fiscal year 2018-19 or the near future, it is important to maintain solid reserves and have a balanced spending plan to receive excellent bond ratings. Good ratings will ultimately help the City to reduce interest costs. The Five-Year Capital Improvement Program (CIP) has been updated to reflect new projects, grant awards, and allocations between projects and funds. This staff report summarizes the budget highlights, and the budget message in the proposed budget provides more analysis about the economic conditions, revenues, expenditures, and reserves.

## **ANALYSIS**

### **Budget Overview**

This budget focuses on long-term fiscal sustainability and reflects strategies to reduce costs and pay down the City's unfunded pension liability. The fiscal strategies utilized to balance this budget are consistent with the City's budget philosophy for long-range planning and effective program management. The goal is to enhance the City's financial security into the future recognizing that expenditures are expected to outpace revenue growth in the next several years, especially due to rising pension costs. While a revenue study is underway to identify viable revenue options, the 2017-19 budget is balanced with cost savings.

The Citywide operating expenditures exceed \$85 million and \$73 million for fiscal years 2017-18 and 2018-19, respectively. Together with the capital budget, the expenditures are \$106 million for fiscal year 2017-18 and \$97 million for fiscal year 2018-19. The General Fund proposed expenditures/revenues are \$40.3 million for each of the two budget years.

The General Fund Five-Year Financial Projection shows that the expenditure growth will outpace revenue growth resulting in long-term structural deficits. The long-term forecast reflects the proposed cost reductions approved by the City Council on July 25, 2017 (as described in the Budget-Balancing Strategies section below) and the expected savings from the paydown of pension debt. The 2017-19 budget is balanced after incorporating the cost reductions and adjusting certain revenue and expenditure items. The deficits in fiscal years 2019-20 and 2020-21 are projected to be \$1.9 million and \$3.6 million.

### **2017-19 Budget-Balancing Strategies**

The 2017-19 General Fund budget was balanced with staffing and service reductions, as well as expected savings from the paydown of pension debt in fiscal year 2017-18. The budget also reflects a 10% fee increase in fiscal year 2018-19 for the Child

Development Center to stabilize General Fund subsidies. These budget-balancing strategies were approved by the City Council on July 25, 2017. The cost reductions consist of contracts and other operating costs, staffing allocation to other funds, vacant positions and occupied positions as summarized below. The cost reductions excluded the K-9 program for the Police Department (approximately \$31,000/year). After further evaluation, staff concluded that it is important to retain this program to reduce officer safety risk. Staff recommends to restore this program. The budget for ECCL operating expenses was reduced to offset the expense for the K-9 program. A Summary of Program Reductions is included in the proposed budget attached to this staff report.

Staff reductions are not expected in fiscal year 2017-18 except for the Assistant City Manager position. Management is currently reviewing vacant positions that fill a critical need for the organization. This process along with potential individual department's reorganization efforts may identify opportunities for those employees whose positions may be eliminated if the City's financial conditions are not improved.

#### Summary of Cost Reductions

	Number of Positions	FY 17-18	FY 18-19
Contracts and other operating costs		\$ (97,713)	\$ (87,120)
Staffing allocation to other funds		(187,153)	(293,478)
Vacant positions	7 FTEs plus part-time hours (1 FTE)	(616,830)	(671,684)
Occupied positions	7 FTEs	(181,645)	(980,862)
Total		\$ (1,083,342)	\$ (2,033,145)

FTE = Full-time equivalent

This City is proactive in managing its pension obligations and has set aside \$13 million in pension reserves. In July 2017, the City Council directed staff to pay down \$4 million of Police Tier I unfunded pension liability in fiscal year 2017-18 and invest the remaining balance in a Section 115 Pension Trust. Expected savings are incorporated into the five-year projection: \$68,000 for FY18-19, \$127,000 for FY19-20, and \$186,000 for FY20-21. The paydown savings are estimated to be \$11.2 million over a 30-year period.

#### Budget Highlights

The City currently enjoys a sound financial condition. During recent periods of budget surplus, the City has strategically invested in prudent reserves to ensure the continuity of services during economic downturns and as a contingency for unexpected events. This budget retains a 50% economic uncertainty reserve to provide flexibility to sustain services during inevitable economic cycles.

However, despite its sound reserves, the City faces emerging long-term financial conditions that are impacting the City's ability to balance its annual operating budget going forward. Most notably, these changes include 1) the slowing of tax revenue growth as consumers evolve their buying habits; and 2) sharply increasing pension funding requirements from the CalPERS pension system due to lowering of investment income assumptions. Like many other cities across the state, the City needs to control expenditures and increase revenues to sustain vital services and programs going forward. The 2017-19 budget was developed based on the assumption that the economy will remain healthy, meaning recession factors are not built into this budget. If there is a slowdown in the economy during this budget cycle, the City may need to draw into the Economic Uncertainty reserves.

### ***Recommended Transfers of General Fund Unassigned Fund Balance to Other Funds/Programs***

Due to budget constraints, staff implemented fiscal strategies to control expenditures in fiscal year 2016-17, including freezing vacant positions and reducing operating costs (professional services, supplies, printing, etc.); departments further deferred hiring of several vacant positions to achieve greater savings; one-time contributions/costs that were budgeted for pension benefits or special activities were cancelled; to preserve funding for General Fund operations, the contribution to the Child Development Center reflects actual subsidy for the year instead of budgeted subsidy, which is a change of accounting practice from prior years; to match program activities, certain budgeted equipment purchases and contract services will incur in fiscal year 2017-18 instead of fiscal year 2016-17. In addition, staff used proactive revenue strategies to collect business license payments. Staff had planned to redirect these unspent resources to support various city programs in anticipation of budget challenges in the next several years (as described in the Long-Term Forecast section below). Staff intended to plan strategically for the future to relieve pressure on the General Fund. Fiscal year 2016-17 revenues and expenditures are projected to be \$39.7 million. Note that fiscal year 2016-17 results remain estimates because certain revenues and invoices for June 2017 have not been received. Actual results may be different from the projections.

In the last budget cycle and the current budget cycle, the City identified several key program areas that are in need of funding. Additional resources were not allocated to these programs due to funding limitations. Staff proposes to divert fiscal year 2016-17 available resources to these programs to support future services. Proposed transfers are to be recorded in fiscal year 2016-17. These one-time transfers will eliminate the need to increase General Fund contributions in 2017-19.

### **Recommendations**

#### **1. Library Services**

The City currently does not operate a library, but contracts with the City of

Oakland for the services. The annual cost is \$120,000. This amount does not represent the full cost of services that are provided by Oakland, which is nearly \$800,000. Oakland City Officials advised staff that Oakland will take a phased-in approach to increase the charge to market rate over a multi-year period, but costs will continue to increase over time due to inflation as well. While awaiting Oakland's proposal, staff made conservative estimates for the 2017-19 budget. Staff will also evaluate other alternatives to identify the most cost-effective way to provide library services to the community. Regardless of how the services will be delivered, start-up costs and ongoing costs will be required to support the program. Staff proposes to transfer \$500,000 into the Community Programs Fund to sustain future services. The funds will be used to cover the expected increases.

2. Emeryville Center of Community Life (ECCL) – Capital Reserve Contributions  
The City/School project was successfully completed in early fiscal year 2016-17, and this is the first year that the City and the Emeryville Unified School District jointly operated the Center. Besides the annual operating and maintenance costs, the City is required to make annual contribution towards capital replacements. The capital replacement schedule calls for annual contribution of less than \$5,000 in the first five years. However, starting the 6<sup>th</sup> year the annual contribution will be over \$60,000 and will continue to increase in future years. It has been the City's practice to make annual General Fund contributions to the Major Maintenance Fund to fund major maintenance and replacement costs for City owned facilities. Contributions to the capital reserve fund need to start in this budget cycle to cover future increases. In light of the budget challenges, additional contributions will further burden the General Fund in this budget cycle and the next budget cycle. Staff proposes to make a one-time transfer of \$400,000 to the ECCL Fund in fiscal year 2016-17 to relieve General Fund pressure.
3. Support for Information Technologies (IT)  
Funds in the Information Technology Fund are used to support IT capital replacements/purchases and computerized systems for Community Development, Public Works, Police Department, and other citywide programs such as the Records Management System. Funding sources are from annual General Fund contributions and technology fees collected from development projects. Community Development lowered the revenue estimates based on expected development projects in the next several years prompting a General Fund contribution to support the current projects. Staff proposes to transfer \$1,000,000 from the General Fund into the Information Technology Fund. This will enable the General Fund to maintain the annual contribution at the current level of approximately \$200,000 through fiscal year 2020-21.
4. Earthquake Insurance/Disaster Fund

The Earthquake Reserve Fund was established in FY 2002-03 and accounts for resources set aside for potential severe seismic incidents, and the current fund balance is approximately \$1.3 million. Per our insurance broker, the recommended insurance coverages are \$5 million, \$10 million, and \$15 million. The City's reserve balance appears to be low compared to the minimum recommended coverage. In fiscal year 2015-16, the City Council directed staff to increase the reserve balance over time. Staff proposes to transfer \$550,000 into the reserve fund and change the fund description to Disaster Fund. Besides earthquakes, the reserve will be used to respond to disasters such as fire, floods, and terrorist attacks.

5. Code Enforcement Program

The City's Code Enforcement Program focuses on resolving health, safety, and public nuisance problems that may adversely affect the quality of life for citizens of Emeryville. From time to time, the City may encounter significant code enforcement activities that require the City to cover the costs and the costs may be recovered through property tax liens. Currently there is no dedicated funding source to support significant activities, and the City has to draw into the General Fund reserves to cover these costs. Staff proposes to establish a Code Enforcement Fund and transfer \$300,000 into the new fund to cover anticipated costs.

6. Legal Services - Litigation Fund

The Litigation Fund was established to account for all litigation expenses of the City, and the current fund balance is slightly below \$1.5 million. Staff conducted an analysis of this fund taking into consideration the current and expected legal activities and concluded that the fund balance can be depleted quickly if there are significant and unforeseen legal expenses. An increase is necessary to maintain an adequate fund balance to provide for unanticipated and unpredictable litigation initiated by or brought against the City. Staff recommends transferring an additional \$500,000 to the Litigation Fund in addition to the \$150,000 budgeted transfer. This will avoid substantial increase in annual General Fund contributions in this budget cycle and next budget cycle.

The recommended transfers for various programs are summarized below.

### Proposed FY 16-17 General Fund Transfers

	Proposed Amounts
Community Programs - Library Services	\$ 500,000
ECCL - Capital Reserve Contributions	400,000
Information Technologies	1,000,000
Disaster Fund	550,000
Code Enforcement Program	300,000
Litigation Fund *	500,000
	<hr/>
	\$ 3,250,000

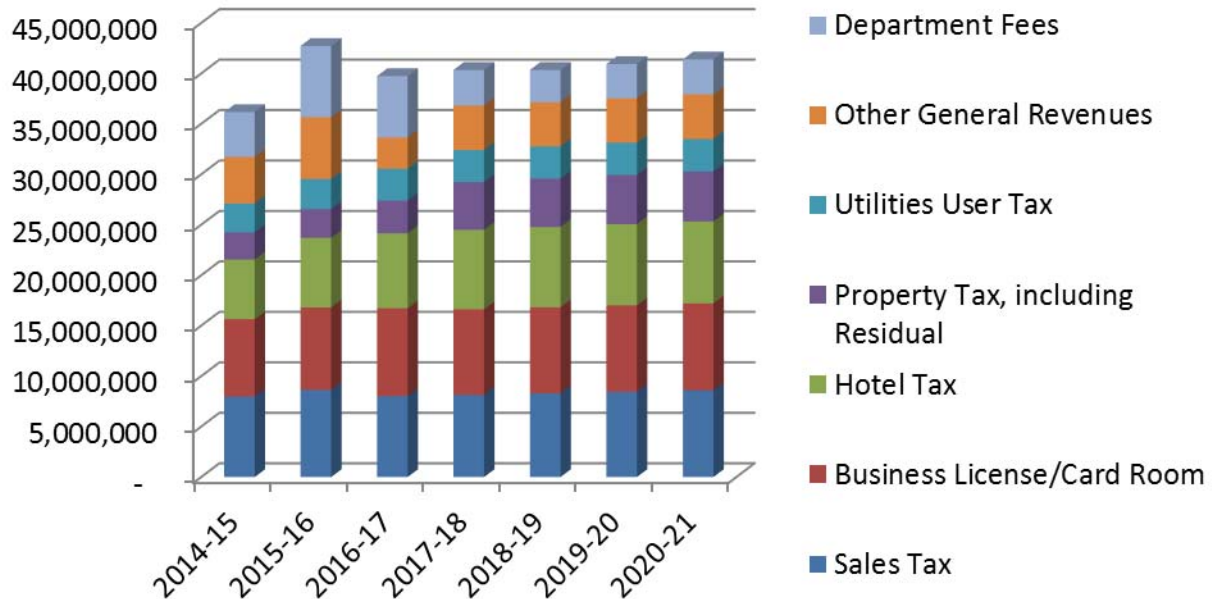
\* In addition to the \$150k budgeted transfer.

### Revenue Projections

General Fund revenue base has been subject to significant year-to-year fluctuations because of the recent expansion of the real property transfer tax; the opening of a new hotel with related Transient Occupancy Tax (TOT); and transaction-related development revenues. Fiscal year 2016-17 General Fund revenues are projected at \$39.7 million, which is in line with the amended budget but lower than the fiscal year 2015-16 actual of \$43.7 million. Note that these 2016-17 results remain estimates and are subject to achieving tax revenues that will become final when the State Board of Equalization releases final June 30, 2017 sales tax results in September 2017.

The General Fund will benefit from two new revenue sources in the 2017-19 budget cycle. Based upon policy direction adopted with the 2016-18 budget, 25% of Residual Tax Increment will be dedicated to support General Fund operations. These are unused tax increment revenues from the former Redevelopment Agency that now flow back to taxing agencies since the 2012 State-wide redevelopment dissolution. This new General Fund revenue is now projected at \$1.4 million and is higher than prior estimates due to the recent State denial of the Successor Agency's funding of the Corporation Yard remediation project. A second new revenue in this budget cycle is a \$500,000 transit grant to support the Public and Business Improvement District (PBID) Emery-Go-Round shuttle service. The grant has been awarded for two years. For planning purposes, this projection optimistically assumes the grant will continue through 2020-21 based upon long-term planning projections provided by the grantor. Total General Fund tax and fee revenues for 2017-18 and 2018-19 are expected to increase to \$40.3 million, a 1.5% growth from 2016-17. 2019-20 and 2020-21 revenues are expected to reach \$40.9 million and \$41.3 million, a 3% cumulative growth from 2018-19. Analysis of significant revenue categories is included in the budget message attached to this staff report. The chart below shows the General Fund revenue trends.

### General Fund Revenue Trends

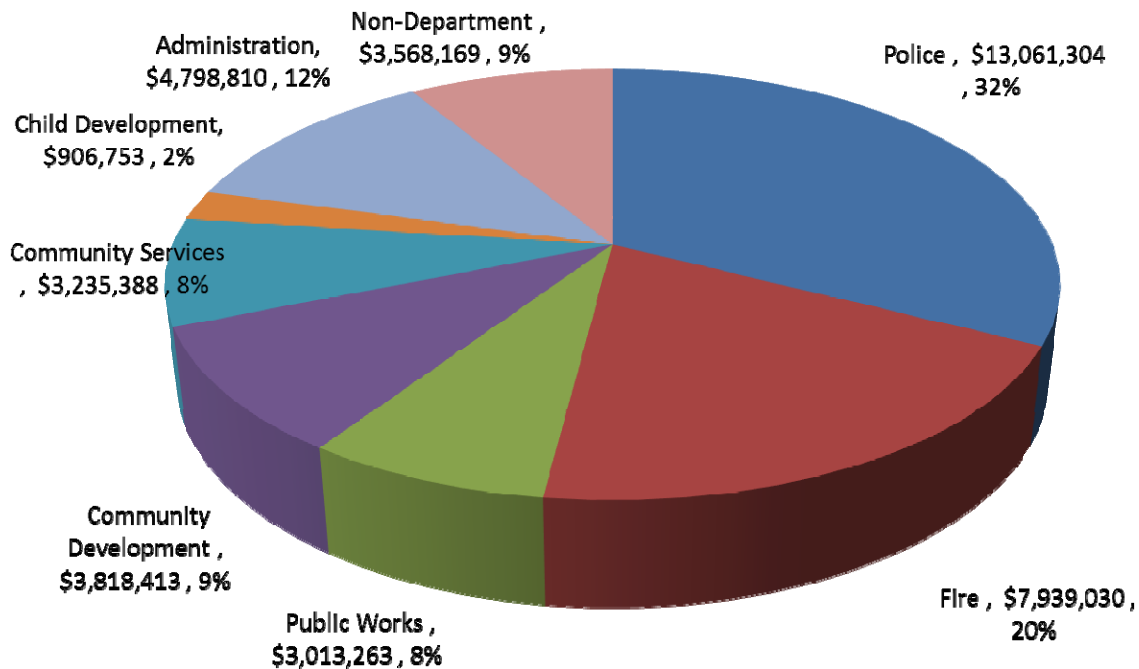


### Expenditure Projections

General Fund expenditures total \$40.3 million in each of the two budget years, and expenditures are expected to reach \$42.9 million in 2019-20 and \$44.9 million in 2020-21. The pie chart below shows the 2017-18 General Fund expenditures by program. Police and Fire comprise more than 50% of the General Fund budget. As a service provider, the primary driver of the City's cost of services is its employee salary and benefit structure. City-wide salary and benefit costs are projected to grow from \$24.9 million in 2017-18 to \$28.4 million in 2020-21. The General Fund share grows from \$21.5 million to \$24.1 million during this period. Analysis of significant expense categories is included in the budget message attached to this staff report.



### 2017-18 General Fund Expenditures by Department



### Capital Improvement Program (CIP)

The five-year CIP has been updated to reflect new projects, grant awards, and allocations between projects and funds. The five-year program totals \$144 million, and appropriations of \$44 million for 2017-19 are included in this budget. Of the \$144 million, \$20 million is in the unfunded category. Funding needs to be identified to implement those projects. Funding for CIP projects relies on available fund balances and projected revenues.

To insulate the annual operating budget from long-term capital asset support costs, the City established a \$5 million Infrastructure Reserve and a \$2.5 million Implementation Reserve in the General Capital Fund in June 2016. The Infrastructure Reserve is to ensure funds are available to support the long-term stewardship of the City's capital infrastructure; the Implementation Reserve is to ensure that the City can deliver and implement its capital improvement program. The CIP projects are presented in the Capital Funds section of the proposed budget.

Changes were made to various projects to reflect updated costs, project delivery schedules, and project scopes, and significant changes are described here. Additional tax increment revenues received in FY 16/17 and expected revenues for the next four years have been set aside for the Corporation Yard project due to the denial of the

remediation plan by the Department of Finance, and the revenues are estimated at \$6.2 million. The City may be required to clean up the site even if funding from the Successor Agency is not available. The City was successful in securing several grant awards from the Alameda County Transportation Commission and other agencies, and these funds have been added to projects such as the South Bayfront Bridge, North Hollis Paid Parking and Transportation Demand Management and the Bike Share Stations projects.

The City Council gave staff authority to remove discretionary projects to relieve pressure on the General Fund. Staff proposes to remove the Carport Solar Installation project and redirect a portion of the funding to the Electric Vehicle Chargers project (\$125k). Staff also proposes to remove the Halleck Beach Dog Park project and redirect funding to the Temescal Creek Park (approximately \$280k). The scope of the EV Charging Stations has been modified to include the installation of three stations and the scope of the Temescal Creek Park Improvements is being reviewed to see if important safety improvements to lights and walkways can be expedited.

Three new projects have been added, San Pablo Mid-Block Crossing, the Powell Corridor Traffic Safety Study, and the San Pablo Avenue Supportive Housing Project. Funding for the San Pablo Mid-Block Crossing will come from new streets and roads allocations from SB-1. The preferred project scenario for the San Pablo Avenue Supportive Housing Project would include 39 units of below market rate supportive housing units, 5,188 square feet for the Emeryville Community Action Program (ECAP) and 1,598 square feet for other community services, with 16 parking spaces. The site is currently occupied by ECAP and commercial uses and will require remediation. This project is partially unfunded and a portion of the funding will come from the City's Housing Fund/tax increment revenue.

## **REVIEW BY CITIZENS COMMITTEES**

The proposed budget will be presented to the Budget Advisory Committee for review on September 1, 2017. Staff will present the Committee's comments and recommendations to the Council at the September 5<sup>th</sup> meeting.

## **NEXT STEPS**

After receiving City Council's feedback, staff will finalize the budget and submit to the Council for consideration on September 19, 2017.

**PREPARED BY:** Susan Hsieh, Finance Director

**APPROVED AND FORWARDED TO THE CITY COUNCIL OF  
THE CITY OF EMERYVILLE BY:**



---

Carolyn Lehr, City Manager

**ATTACHMENT**

1. Draft Proposed Budget for Fiscal Years 2017-18 and 2018-19