

**MEMORANDUM**

Finance and Administrative Services Department

DATE: December 13, 2022

TO: Honorable City Council

FROM: Ann Trinh, Senior Financial Analyst
Grace Zheng, Assistant Finance and Administrative
Services Director
Jesse Takahashi, Finance and Administrative Services Director

VIA: Kimbra McCarthy, City Manager

SUBJECT: **Analysis of Fiscal Year 2021-22 Audited Financial Results for the General Operating Fund and General Fund Available Balance**

PURPOSE

To provide an analysis of the Fiscal Year 2021-22 audited financial results for the General Operating Fund and General Fund available balance (including one-time revenues and expenditure savings).

BACKGROUND

The General Operating Fund (GOF) accounts for recurring unrestricted revenues and general operating expenditures. It is a subset of, and distinguished from, the General Fund, which accounts for total unrestricted revenues and total General Fund expenditures, including reserves and nonrecurring revenues and expenditures in nonoperating accounts.

This memorandum provides an analysis of the audited GOF financial results for Fiscal Year 2021-22. Some amounts will not match the Annual Comprehensive Financial Report (ACFR) as certain revenue and expenditure reclassifications have been made for financial statement reporting purposes. In addition, the ACFR groups all General Fund revenues and expenditures together, including reserves. The City defines “operating” as the recurring revenues and expenditures supporting ongoing City services. These classification differences do not affect the evaluation of the GOF’s financial position. For purposes of this analysis, one-time General Fund revenues and expenditures have been reclassified to conform to the City’s definition of “operating” and are presented separately.

ANALYSIS

Fiscal Year 2021-22 GOF Audited Financial Results

The Fiscal Year 2020-21 Audited and Fiscal Year 2021-22 Adopted Budget, Adjusted Budget, and Audited results for the GOF are as follows (dollars in thousands):

	<u>2020-21</u> <u>Audited</u>	<u>2021-22</u> <u>Adopted</u> <u>Budget</u>	<u>2021-22</u> <u>Adjusted</u> <u>Budget</u> ⁽¹⁾	<u>2021-22</u> <u>Audited</u>	Variance of Audited to Adjusted
Revenues	\$143,706	\$146,412	\$147,748	\$163,376	\$15,628
Expenditures ⁽²⁾	(136,811)	(150,804)	(154,809)	(145,825)	8,984
Excess ERAF ⁽³⁾	6,841	5,836	5,836	-0-	(5,836)
Rebudgets ⁽⁴⁾	<u>(5,235)</u>	<u>-0-</u>	<u>3,165</u>	<u>13</u>	<u>(3,152)</u>
Operating Balance	<u>\$ 8,501</u>	<u>\$ 1,444</u>	<u>\$ 1,940</u>	<u>\$ 17,564</u>	<u>\$15,624</u>

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- (1) The Adjusted Budget includes the Adopted Budget and encumbrance carryovers from prior fiscal years, increases for reimbursed expenditures, grants and donations, and any budget adjustments approved during the fiscal year.
- (2) Amounts are net of budget savings of \$4.0 million for both Fiscal Years 2020-21 and 2021-22.
- (3) Fiscal Years 2020-21 Audited and 2021-22 Adopted/Adjusted Budget include \$6.8 million and \$5.8 million Property Tax—Excess Education Revenue Augmentation Fund (ERAF) revenue, respectively, in order to ensure the budget was balanced. This revenue is considered one-time in nature and was recorded in the General Non-Operating Fund (GNOF) as one-time revenue in prior fiscal years. Fiscal Year 2021-22 has been moved to the GNOF as it was no longer needed to balance the budget.
- (4) Rebudgets include encumbrances and grant/donation carryovers from the prior fiscal year and changes in assets and liabilities for audited results.

The Fiscal Year 2021-22 total audited revenues are \$15.6 million (10.6%) over the Adjusted Budget, \$17.0 million (11.6%) over the Adopted Budget, and \$19.7 million (13.7%) higher than the Fiscal Year 2020-21 Audited. The Fiscal Year 2021-22 total audited expenditures are \$9.0 million (5.8%) below the Adjusted Budget, \$5.0 million (3.3%) below the Adopted Budget, and \$9.0 million (6.6%) higher than the Fiscal Year 2020-21 total Audited expenditures.

The economic impacts of COVID-19 have been ever-changing, but mostly positive, as recovery from the pandemic continues with the gradual return of normal activities. Recreation activities are coming back strong with record-high registration rates for recreation camps and classes. Some revenues, such as Sales Tax and Transient Occupancy Tax (TOT) revenue, are recovering

but still are not fully back to prepandemic levels. Most notable is the loss of TOT revenue, \$2.6 million lower in Fiscal Year 2021-22 compared to Fiscal Year 2018-19, the last full year prior to the pandemic. It is fortunate the City has generated a strong operating balance as it provides an opportunity to add critical positions and contribute to the City’s other priorities, including unfunded liabilities for CalPERS pensions.

A discussion of variances by revenue and expenditure categories follows.

Revenues

The Fiscal Year 2020-21 Audited and Fiscal Year 2021-22 Adopted Budget, Adjusted Budget, and Audited results for GOF revenues are as follows (dollars in thousands):

	2020-21 <u>Audited</u>	2021-22 Adopted <u>Budget</u>	2021-22 Adjusted <u>Budget</u>	2021-22 <u>Audited</u>	Variance of Audited to Adjusted
Operating Revenues:					
Property Taxes	\$ 59,783	\$ 60,272	\$ 60,272	\$ 63,996	\$ 3,724
Sales Tax	18,058	18,477	18,477	23,376	4,899
Other Local Taxes	13,717	16,775	16,775	18,663	1,888
Use of Money and Property Licenses, Permits, and Franchise Fees/Fines and Forfeitures	22,195	23,014	23,014	24,530	1,516
	5,677	6,767	6,767	5,936	(831)
Intergovernmental	782	738	738	1,986	1,248
Charges for Services	1,941	2,099	2,099	3,037	938
Miscellaneous Revenues	4,358	1,781	3,074	4,133	1,059
Interfund Revenue and Transfers	<u>17,195</u>	<u>16,489</u>	<u>16,532</u>	<u>17,719</u>	<u>1,187</u>
Total Operating Revenues	<u>\$143,706</u>	<u>\$146,412</u>	<u>\$147,748</u>	<u>\$163,376</u>	<u>\$15,628</u>

A summary of revenues by category follows:

- The July 1, 2021 City GOF property tax roll saw increased secured and unsecured assessed values (AV), including recaptured Proposition 8 value and tax roll reductions from resolved appeals, resulting in a net 6.1% increase compared to the prior year tax roll. Overall, AV in the City increased a net 8.1%, which is the highest among the 15 cities in the County. This presented a better outlook than staff originally expected as developers showed continued interest in constructing commercial and residential buildings. Property tax revenues totaling \$64.0 million are \$3.7 million (6.2%) higher than budget and \$4.2 million (7.0%) more than the Fiscal Year 2020-21 Audited. The variance between budget and actual is

primarily due to the higher-than-budgeted secured and property tax in lieu of Vehicle License Fees (VLF).

- Sales tax revenues are \$4.9 million (26.5%) above budget and \$5.3 million (29.4%) higher than the Fiscal Year 2020-21 Audited. This is primarily due to strength in new automobile sales, fuel/service stations, and quicker-than-expected rebound from restaurants as the economy continued to recover.
- Other Local Taxes are \$1.9 million (11.3%) above budget and \$4.9 million (36.1%) higher than the Fiscal Year 2020-21 Audited. The comparison to Fiscal Year 2020-21 Audited is primarily due to \$2.5 million higher TOT revenues and \$2.1 million more Business License Tax revenue resulting from the final year of the restructured Business License Tax being phased in over three years. Although TOT revenues increased, travel and, in particular, business travel, remains impacted by the pandemic affecting hotel occupancy and the resulting revenue.
- Use of Money and Property revenues, including both Investment Earnings and Rents and Leases, are \$1.5 million (6.6%) above budget and \$2.3 million (10.5%) higher than the Fiscal Year 2020-21 Audited. Investment Earnings are \$276,000 (10.5%) above budget and essentially the same as the Fiscal Year 2020-21 Audited. The Federal Open Market Committee (FOMC) raised the benchmark interest rate three times during Fiscal Year 2021-22, which increased its target benchmark range of 1.50% and 1.75%. This positively impacted the City's interest earnings and will have a greater impact on future fiscal years as lower-yielding securities mature. Rents and Leases revenues are \$1.2 million (6.1%) above budget and \$2.3 million (12.1%) more than Fiscal Year 2020-21 Audited. This is primarily due to standard annual rent adjustments per lease agreements and percentage rent revenue for the Ameswell office lease. Included in Rents and Leases revenues is approximately \$2.2 million in revenue generated from the Ameswell development, which is earmarked to help fund the Public Safety Building project.
- Licenses, Permits, and Franchise Fees/Fines and Forfeitures are overall net \$831,000 (12.3%) below budget and \$259,000 (4.6%) higher than the Fiscal Year 2020-21 Audited. The variance to the budget is primarily due to less-than-anticipated franchise fees and parking violation revenues; the variance to the prior fiscal year Audited is primarily due to an increase in franchise fees.
- Intergovernmental Revenues are \$1.2 million higher than budget and Fiscal Year 2020-21 Audited, primarily due to a grant awarded to the Center for the Performing Arts.
- Charges for Services are \$938,000 (44.7%) and \$1.1 million (56.5%) above budget and the Fiscal Year 2020-21 Audited, respectively. Revenues in this category are mainly derived

from City Recreation programs and miscellaneous other services. The variance is primarily due to the strong recovery from Recreation and the Center for the Performing Arts.

- Miscellaneous Revenues are \$1.1 million (34.5%) above budget, primarily resulting from one-time donations and reimbursements that are not included in the Adopted Budget. The City budgets various donations and reimbursements only if they are ongoing in nature. A significant portion of the reimbursements was a result of strike team services rendered for wildfires throughout the State. Compared to Fiscal Year 2020-21 Audited, Miscellaneous Revenues are \$225,000 (5.2%) lower, primarily as a result of less reimbursements received in Fiscal Year 2021-22 from strike team reimbursements.
- Interfund Revenues and Transfers are \$1.2 million (7.2%) above budget and \$524,000 (3.0%) higher than the Fiscal Year 2020-21 Audited, primarily as a result of higher Capital Improvement Projects (CIP) administrative overhead.

Expenditures

The Fiscal Year 2020-21 Audited and Fiscal Year 2021-22 Adopted Budget, Adjusted Budget, and Audited results for GOF expenditures are as follows (dollars in thousands):

	<u>2020-21 Audited</u>	<u>2021-22 Adopted Budget</u>	<u>2021-22 Adjusted Budget</u>	<u>2021-22 Audited</u>	<u>Variance of Audited to Adjusted</u>
Operating Expenditures:					
Salaries and Benefits:					
Salaries and All Pays	\$ 68,292	\$ 72,483	\$ 73,200	\$ 71,709	\$1,491
Retirement	21,672	25,834	25,834	22,257	3,577
Health Benefits	9,090	11,803	11,803	9,190	2,613
All Other Benefits	<u>6,875</u>	<u>7,762</u>	<u>7,723</u>	<u>7,082</u>	<u>641</u>
	105,929	117,882	118,560	110,238	8,322
Supplies and Services	17,753	20,086	22,959	18,784	4,175
Capital Outlay/ Equipment Replacement	2,899	2,745	3,199	2,854	345
Interfund Expenditures and Transfers	10,230	13,091	13,091	13,949	(858) ⁽¹⁾
Debt Service	-0-	1,000	1,000	-0-	1,000
Budget Savings	Included	(4,000)	(4,000)	Included	(4,000)
Transfer to GNOF	-0-	-0-	-0-	-0-	-0-
Transfer to GF Reserve	-0-	-0-	-0-	-0-	-0-
CalPERS Contribution	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>
Operating Expenditures	<u>\$136,811</u>	<u>\$150,804</u>	<u>\$154,809</u>	<u>\$145,825</u>	<u>\$8,984</u>

⁽¹⁾ The negative variance is due to higher-than-anticipated revenues received but not budgeted as Ameswell development and excess business license tax revenues are transferred to their respective earmarked reserves and fund. The Ameswell development revenues are transferred to the Budget Contingency Reserve, and 90.0% of the excess business license tax revenue are transferred to the General Fund Transportation Reserve and General Housing Fund.

A summary of expenditures by category follows:

- During Fiscal Year 2021-22, more positions were filled than vacated, and over 60.0% more vacancies were filled in comparison to the prior fiscal year. However, the City has continued the commitment to employee development with over one-third of the vacancies filled through promotion, which resulted in additional vacancies. Despite significantly increased recruitment efforts, there were still many unfilled positions, resulting in a \$8.3 million

(7.0%) favorable variance in Salaries and Benefits compared to Adjusted and \$7.6 million (6.5%) compared to Adopted.

- Historically, the GOF typically realizes savings in Supplies and Services. For Fiscal Year 2021-22, there were savings of \$4.2 million (18.2%) compared to Adjusted and \$1.3 million (6.5%) compared to Adopted. However, of this amount, encumbrances totaling \$2.4 million were identified to be carried over into Fiscal Year 2022-23. Including these encumbrances, the variance to Adjusted Budget would be reduced to \$1.8 million or 7.7%.
- The GOF's \$2.2 million contribution to the Equipment Replacement Reserve occurred as budgeted. The remaining capital outlay has a favorable variance of \$345,000 (36.1%) compared to budget; \$226,000 of this has been encumbered to be expended in Fiscal Year 2022-23.

The budget savings of \$4.0 million takes into consideration the anticipated savings in expenditure accounts. The Fiscal Year 2021-22 Audited amounts indicated in the table do not include a total of \$2.6 million of encumbrances outstanding as of the end of the fiscal year. In accordance with the City Charter, appropriations for lawful encumbrances remaining at the end of each fiscal year are reappropriated in the following fiscal year.

Expenditures by Department

A summary of the GOF audited expenditures compared to Adjusted Budget by department are as follows (dollars in thousands):

	2021-22 Adjusted <u>Budget</u>	2021-22 <u>Audited</u>	<u>Encumbrances</u>	Variance of Audited Plus Encumbrances <u>to Adjusted</u>	% Savings from Adjusted <u>Budget</u>
Department:					
City Council	\$ 424	\$ 254	-0-	\$ 170	40.1%
City Clerk	985	896	-0-	89	9.0%
City Attorney	2,621	2,235	72	314	12.0%
City Manager	4,673	3,548	346	779	16.7%
Human Resources Information	2,631	2,552	79	-0-	0.0%
Technology	6,718	5,527	353	838	12.5%
Finance and Administrative Services	7,633	6,055	295	1,283	16.8%
Community Development	2,015	1,811	108	96	4.8%
Public Works	12,364	11,595	433	336	2.7%
Community Services	19,069	16,501	311	2,257	11.8%
Library	7,301	5,827	160	1,314	18.0%
Fire	29,526	29,214	240	72	0.2%
Police	46,073	43,289	238	2,546	5.5%
Nondepartmental ⁽¹⁾	16,776	16,521	-0-	255	1.5%
Budget Savings	<u>(4,000)</u>	<u>Included</u>	<u>-0-</u>	<u>(4,000)</u>	100.0%
Total Operating Expenditures	<u>\$154,809</u>	<u>\$145,825</u>	<u>\$2,635</u>	<u>\$6,349</u>	4.1%

⁽¹⁾ Nondepartmental expenditures include Interfund Transfers for equipment replacement and Interfund Expenditures and Transfers.

All departments ended Fiscal Year 2021-22 with expenditures below the Adjusted Budget.

Fiscal Year 2021-22 GOF Balance Available

As previously discussed, the City's GOF ended the 2021-22 fiscal year with a positive operating balance of \$17.6 million. The table below details the General Fund balance, including one-time

revenues and expenditure savings, budgeted transfers, and limited-period expenditure allocations (dollars in thousands):

GOF Balance from Fiscal Year 2021-22	\$17,564
Remaining Available Balance from Prior Fiscal Years	5,012
Midyear Allocations Approved by City Council	(1,275)
One-Time Revenues and Expenditure Savings:	
Property Taxes—Excess ERAF	8,260
Unspent Limited-Period Expenditures	2,521
Miscellaneous Revenues	1,028
Child-Care Center Rent	<u>201</u>
Subtotal	<u>\$33,311</u>
Allocations in the Fiscal Year 2022-23 Adopted Budget:	
Limited-Period Expenditures	(3,755)
Compensated Absences Reserve	(4,020)
CIP Reserve	(3,000)
Strategic Property Acquisition Reserve	(3,000)
Development Services Fund	(2,000)
Public Safety Building Reserve	(1,000)
Sustainability Program	(1,000)
Subtotal of Allocations	<u>(17,775)</u>
Remaining Unallocated Balance Available	<u>\$15,536</u>

Including the GOF balance, the remaining balance available from prior fiscal years less midyear allocations approved by the City Council, one-time revenues, and expenditure savings, there was a total of \$33.3 million available for allocation through Fiscal Year 2021-22.

Allocations in the Fiscal Year 2022-23 Adopted Budget include new limited-period expenditures of \$3.8 million; transfers of \$4.0 million to the Compensated Absences Reserve, \$3.0 million to the CIP Reserve, \$3.0 million to the Strategic Property Acquisition Reserve, \$2.0 million to the Development Services Fund, \$1.0 million to the Public Safety Building Reserve, and \$1.0 million to the Sustainability Program. This results in a **remaining unallocated balance of \$15.5 million as of June 30, 2022.**

CONCLUSION

Total Fiscal Year 2021-22 GOF revenues are \$163.4 million, \$15.6 million (10.6%) over the Adjusted Budget and \$17.0 million (11.6%) over the Adopted Budget. Total Fiscal Year 2021-22 GOF expenditures are \$145.8 million, \$8.9 million (5.8%) below the Adjusted Budget and \$5.0 million (3.3%) below the Adopted Budget. This does not include the \$2.6 million in encumbrances outstanding at the end of Fiscal Year 2021-22. The GOF ended Fiscal Year 2021-22 with a positive operating balance of \$17.6 million, which provided critical funding for Fiscal Year 2022-23 limited-period expenditures and transfers to reserves. The remaining unallocated balance is \$15.5 million.

An updated estimate of the City's financial position for Fiscal Year 2022-23 and preliminary projections for Fiscal Year 2023-24 will be presented to Council in February 2023 with the Midyear Budget Status Report.

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