



M E M O R A N D U M
F i n a n c e D e p a r t m e n t

DATE: April 11, 2006

TO: City Council

FROM: Dave Warren
Director of Finance

SUBJECT: MID-YEAR BUDGET STATUS AND FINANCIAL OUTLOOK REPORT

RECOMMENDATION:

Acknowledge and file the Mid-Year Budget Status and Financial Outlook Report.

DISCUSSION:

Tonight, staff will present a status update on the City's Operating and Capital Improvement Budgets and the overall financial position of the City. We will cover the following topics:

- Recap budget challenges
- Discuss City's economic environment
- Review City's General Fund financial position
- Summarize budget actions
- Discuss Fiscal Year 2005/2006 year-to-date results

ANALYSIS:

The Council adopted the General Fund and Special Fund Operating Budget in June 2005 which included four new positions including one full-time Maintenance Worker I (Public Works), one half-time Office Assistant Assistant II (Community Development/Public Works), one full-time Archive Technician (Administration), and one full-time IT Analyst (Administration). The General Fund Budget was balanced, totaled \$7,454,234, and maintained the \$150,000 contingency for unforeseen expenditures.

The City's independent auditor, Caporicci & Larson, Certified Public Accountants, completed the Fiscal Year 2004/2005 Year-End Audit Report which was presented to the Council on March 14, 2006. The City's Financial Statements received an unqualified opinion.

Budget Challenges. Over the past four years, the City has grappled with escalating personnel costs including rising retirement contributions, health insurance, and worker's compensation premiums. From July 1, 2003 to June 30, 2005, a total of \$884,886 has been transferred from the Economic Impact Reserve (a one-time funding source) to the General Fund to help "smooth" the spikes in personnel costs. The Fiscal Year 2005/2006 General Fund Budget includes another \$399,201 transfer in from the Economic Impact Reserve. This is the first year that the transfer was not increased from the prior year, and the General Fund Budget absorbed the personnel cost impacts for the current year. Due to a more positive trend in revenue streams, the Council authorized a \$100,000 transfer from the General Fund to help restore the Economic Impact Reserve in Fiscal Year 2004/2005.

The City's CalPERS retirement contribution rates have risen dramatically due to poor investment performance over the past four years and mandated pooling of CalPERS agencies with less than 100 eligible employees. Local retirement experience and payroll also affect the City's contribution rates. The City is currently paying \$0.2082 for every dollar of salary for miscellaneous employees and \$0.3220 for every dollar of salary for public safety employees. The contribution rates were \$.0859 and \$0.09 respectively four years ago. The cumulative increase in retirement contributions over the past four years was \$782,705. The General Fund has experienced \$483,316 in rate increases alone. Because the City has less than 100 regular employees who are eligible to participate in the City's retirement system, it was required to join a retirement risk pool with other agencies with similar characteristics effective July 1, 2005. Although staff is optimistic that the risk pool model will help smooth the radical spikes in retirement contributions the City has experienced every ten years or so, we are skeptical that the risk pool will provide contribution rate relief any time soon.

<i>Fiscal Impacts of CalPERS Rate Increase</i>				
<i>Fiscal Year Ending June 30</i>	<i>General</i>	<i>Water</i>	<i>Sewer</i>	<i>Special Revenue</i>
2003	\$69,144	\$7,205	\$9,271	\$15,916
2004	\$121,942	\$9,577	\$15,879	\$46,047
2005	\$144,820	\$13,848	\$24,698	\$69,244
2006	\$147,410	\$12,325	\$29,906	\$45,473
Total	\$483,316	\$42,955	\$79,754	\$176,680

The City has received the latest CalPERS actuarial report which includes the City's Fiscal Year 2006/2007. The miscellaneous employee contribution rate will decrease slightly to \$0.2068 while the safety rate will increase to \$0.3432. Placerville is not alone in having to deal with rising contribution rates, and some cities have actually found ways of reducing their current contribution rates. Staff is in the process of researching available options of reducing the annual costs of retirement while maintaining the same level of benefits to employees. Staff will return to the Council with its finding at a later date.

<i>CalPERS Employer Contribution Rates</i>		
<i>Fiscal Year Ending June 30</i>	<i>Miscellaneous Plan</i>	<i>Public Safety Plan</i>
2003	8.59	9.00
2004	11.84	17.31
2005	16.24	26.25
2006	20.82	32.20
2007	20.68	34.32

Increase in health insurance premiums has also had a major impact to the City's personnel costs. Most City employees are enrolled in the Blue Shield EPO Plan. The Blue Shield EPO premiums rose 23.60% in 2005 and a 10% increase in 2006. The total impact of the premium increase in 2006 was \$182,732. The impact to the General Fund alone was \$124,985. The CalPERS Board will adopt new premiums this June for calendar year 2007. Based on current trends, staff anticipates another relatively mild increase in 2007.

The silver lining to personnel cost drivers this year was worker's compensation insurance premiums.

In recent years, the City experienced two massive 40% increase in worker's compensation premiums; one in Fiscal Years 2002/2003 and the other in 2003/2004. The worker's compensation reform legislation (SB 899) that the State adopted in the Spring of 2004 has begun to provide real relief to Placerville in 2005/2006. The City is a member of the Northern California Cities Self Insurance Fund (NCCSIF) JPA. Placerville's individual premium for 2005/2006 was calculated to be 15% less than the prior year. Actual premium, which is netted by the JPA's risk pool needs was 9% less than the prior year saving the City \$151,359. The savings to the General Fund alone was \$74,431. Staff received preliminary worker's compensation rates from NCCSIF last month or Fiscal Year 2006/2007. If adopted by NCCSIF, the new rates will provide even greater relief to Placerville's 2006/2007 operating budget.

<i>Fiscal Impacts of Health Insurance Premium Increases</i>				
<i>Fiscal Year Ending June 30</i>	<i>General</i>	<i>Water</i>	<i>Sewer</i>	<i>Special Revenue</i>
2006	\$124,985	\$13,409	\$26,146	\$18,192

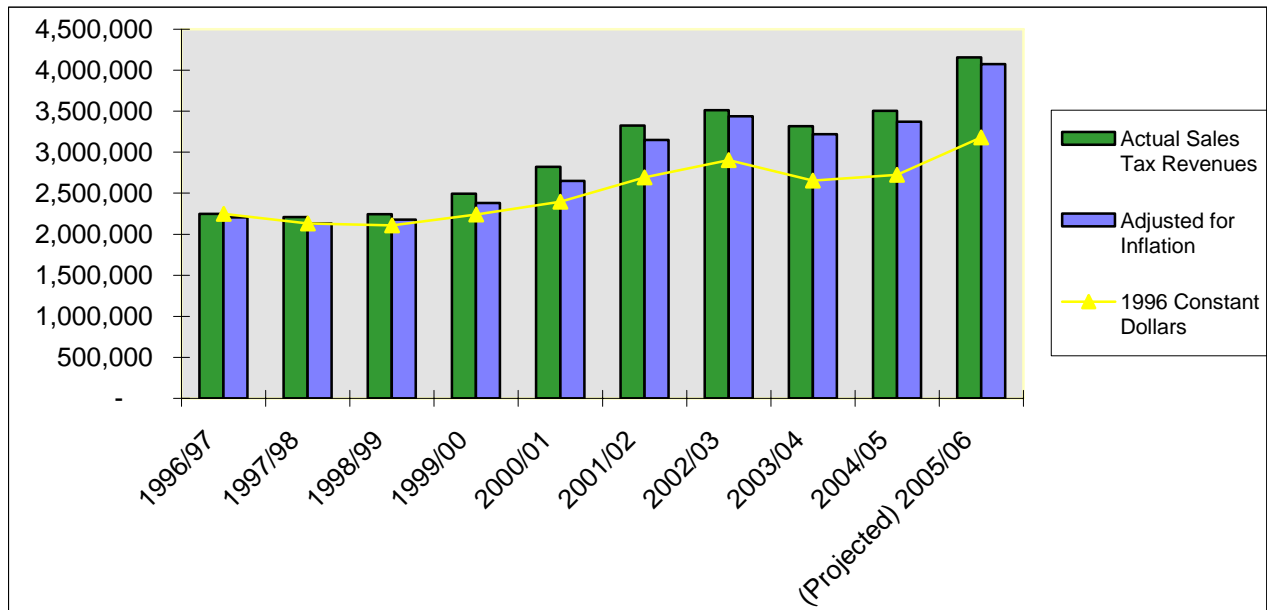
<i>Fiscal Impacts of Worker's Compensation Premium Increases</i>				
<i>Fiscal Year Ending June 30</i>	<i>General</i>	<i>Water</i>	<i>Sewer</i>	<i>Special Revenue</i>
2003	\$95,681	\$21,085	\$38,306	\$18,293
2004	\$85,795	\$16,820	\$28,927	\$27,215
2005	\$10,079	\$1,547	\$3,096	\$3,631
2006	\$(74,431)	\$(10,055)	\$(30,589)	\$(36,284)
4 Year Total	\$117,124	\$29,397	\$39,740	\$12,855

Like other Cities in California, Placerville has been impacted by the State's budget crisis in the form of revenue "grabs" and deferments. Although Proposition 1A (approved by voters in November 2004) provides constitutional protection of City revenues such as property tax, sales tax and vehicle license fees, it did come with a price. Otherwise known as ERAF Shift III, Proposition 1A was a \$1.3 billion hit to local government. The State retained \$103,000 of Placerville's property tax revenue and diverted it to schools in Fiscal Years 2004/2005 and 2005/2006, and Placerville lost a total of \$206,000 in revenues. ERAF III ends in 2005/2006, and Placerville will once again receive the \$103,000 in property tax in 2006/2007.

Economic Environment. There are several economic indicators that point to a growing local economy. The Unemployment rate for the Sacramento region as well as the entire State is at the 1998 level. Although the housing market has slowed, inventory remains low and prices in and around Placerville have held.

The City's VLF apportionment includes 12.76% growth factor that equates to \$74,160 and an additional \$34,833 "true up" for additional revenues earned in 2004/2005. The favorable adjusts equate to a 18% increase in VLF revenues to Placerville. This trend in VLF indicates growth in car sales across the State.

The most significant local economic indicator is Sales Tax receipts which is equivalent to 50% of total General Fund revenues. As of February 2006, 2005/2006 sales tax revenues exceeded 2004/2005 revenues by \$499,718 or 23.24%. Staff projects total sales tax receipts will exceed \$4 million in Fiscal Year 2005/2006 which is equivalent to a 17% increase overall. The favorable increase is attributable to a growing Sales Tax base and incoming businesses like Home Depot.



The projected 17% boost in sales tax receipts is much needed to meet the increases in operating costs due to inflationary impacts. As you can see, the City's sales tax trend has been flat over the past three years. Before 2005/2006, the City's sales tax peaked in 2002/2003. Staff projects 2005/2006 will exceed the 2002/2003 level by 18.20% or \$641,034. However, 2005/2006 projected sales tax is just 9.50% when deflated by accumulated inflation since 1996. In other words a dollar today is worth more than a dollar tomorrow.

Focus on the General Fund. The City's adopted General Fund is balanced and totals \$7,454,234. Based on current trends, staff forecasts General Fund revenues will exceed budget by \$370,968. This is mainly attributable to the boosts in VLF and sales tax revenues mentioned above. Projected expenditures and net transfers out totals \$7,177,412 or \$276,822 less than budget. The favorable expenditure projection is attributable to the City's policy for full exposure budgeting and prudent budget practices by the Council and City management.

	<u>Budget</u>	<u>Forecast</u>	<u>Difference</u>
Audited Beginning Balance 7/01/05	\$ 1,910,878	\$ 1,910,878	\$ -
Revenues	7,454,234	7,825,202	370,968
Expenditures	7,877,413	7,600,591	276,822
Net Transfers In	423,179	423,179	-
Revenues over (under) Expenditures	-	647,790	647,790
Ending Fund Balance 6/30/06[^]	\$ 1,910,878	\$ 2,558,668	647,790

[^]Before reserves and capital set-asides.

The \$647,790 projected General Fund carryover is a one-time funding source that should be limited to one-time uses. Because the carryover is based on a financial forecast as of February 28, 2006, staff cautions the use of these funds until the close of the fiscal year if and when the projections come to fruition.

However, it's a good time for the Council to begin planning for the one-time uses of these dollars. To assist in this process, staff has prepared a draft recommendation for the Council's consideration.

The Fiscal Year 2005/2006 budget includes a transfer in of \$399,201 from the Economic Impact Reserve Fund to "smooth" spikes in health insurance, retirement, and worker's compensation costs over the last four years. This fund transfer has not been made. With the anticipated carryover, the General Fund should be able to absorb the \$399,201 in costs without the fund transfer in. Staff recommends that the \$399,201 transfer in from the Economic Impact Reserve be removed from the General Fund Budget.

Last spring, the Council authorized a fund transfer of \$310,000 from the Fiscal Year 2004/2005 General Fund carryover to the Park Development Fund to cover projected additional costs to the City Pool Reconstruction Project. The \$310,000 was transferred in June 2006. The actual additional costs totaled \$442,367 or \$132,367 more than anticipated last spring. Also, the Park Development Fund cannot absorb these costs at this time. Staff recommends that \$132,367 be transferred from the Fiscal Year 2005/2006 General Fund carryover to the Park Development Fund.

The remaining \$116,222 could be used for additional contingencies or capital project set-asides. Staff's recommendation for the projected carryover is as follows:

Removal of transfer in from Economic Impact Reserve	\$399,201
Addition of transfer out to Park Development Fund	132,367
Additional contingencies or capital project set-aside	<u>116,222</u>
Total	<u>\$647,790</u>

Budget Actions. To date, the Council and the Placerville Finance Authority has taken the following budget related actions:

- Adoption of the Fiscal Year 2005/2006 General Fund/Special Fund Operating Budget
- Adoption of the Fiscal Year 2005/2006 Capital Improvement Program Budget
- Adoption of a new wastewater rate revenue program based on a comprehensive equity study
- Adoption of the Fiscal Year 2005/2006 Sewer Enterprise Fund Operating Budget
- Adoption of four interim budget appropriations for the Water Enterprise Fund
- Authorization of the sale of \$17,215,000 PFA Wastewater System Refinancing and Improvement Project Bonds to be used for the relocation of sewer line along Hangtown Creek and the State-mandated improvements to the Wastewater Treatment Plant
- Authorization of a \$35million SRF loan to be used to construct the State-mandated improvement to the Wastewater Treatment Plant
- Authorized \$300,000 funding agreement with the Air Quality Management District to be used to purchase land and development of Placerville Station II
- Authorized a \$418,000 claim of RSTP revenues to be used for the repayment to SACOG and improvements to Upper Main Street rehabilitation
- Accepted the use of the Fiscal Year 2005/2006 COPS Grant

- Authorized a grant application for rubberized asphalt concrete to be used for the Upper Main Street Rehabilitation Project
- Authorized a \$262,000 claim of RSTP revenues to be used for the Upper Main Street Rehabilitation project
- Appropriated an additional \$37,275,517 for the Waster Water Treatment Plant Upgrade Project based on the recently adopted contract award with Western Water, Inc.

Year-to-Date Results. The delay in opening the new aquatic center had a negative impact to aquatics program revenue this past summer. Staff is optimistic the spring aquatics season will meet revenue expectations. Overall, aquatics revenue is projected to be \$70,000 less than budgeted. This assumption was included in the mid-year forecast presented above.

City staff and consultants are working on completing the new Water Enterprise revenue study. Due to the workload impacts of the 2006 Wastewater Revenue Bond sale, the accelerated schedule of 2005/2006 Year-End Audit, the completion of water revenue program has been delayed. We anticipate coming back to the Council with a proposed Water Enterprise Operating Budget in the next two months.

Since the adoption of the Operating Budget, the Council and management have operated the City in a responsible and prudent manner which has resulted in a healthy estimated carryover this fiscal year. Management was fortunate to have concluded collective bargaining prior to the beginning of the fiscal year. The City implemented year two of the five year salary study plan and COLA for all bargaining groups.

Over the next three months, staff anticipates City operating costs to be well within the existing operating budget.

Dave Warren
Director of Finance

Reviewed and Approved

John Driscoll, City Manager/City Attorney